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No.

Supreme Court, U.S.

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IN THE
Supreme Court of the United States

OCTOBER TERM, 1989

INDEPENDENT INSURANCE AGENTS OF AMERICA, INC.,
NATIONAL ASSOCIATION OF CASUALTY AND SURETY
AGENTS, NATIONAL ASSOCIATION OF LIFE UNDERWRIT-
ERS, NATIONAL ASSOCIATION OF PROFESSIONAL INSUR-
ANCE AGENTS, NATIONAL ASSOCIATION OF SURETY
BOND PRODUCERS, NEW YORK STATE ASSOCIATION OF
LIFE UNDERWRITERS, INDEPENDENT INSURANCE AGENTS
OF NEW YORK, INC., AND THE PROFESSIONAL INSUR-
ANCE AGENTS OF NEW YORK, INC.,

Petitioners,
v.

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM,
Respondent,

MERCHANTS NATIONAL CORPORATION,
Intervenor.

**PETITION FOR A WRIT OF CERTIORARI TO THE
UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT**

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April 18, 1990

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QUESTIONS PRESENTED *

1. Whether a reviewing court must apply a deferential standard of review to an administrative interpretation of a statute merely because the statutory language does not neatly answer the question presented to the court in a single sentence or paragraph.

2. Whether the nonbanking limitations of the Bank Holding Company Act, 12 U.S.C. § 1843, apply when a bank holding company engages in nonbanking activities through the direct ownership and operation of a state-chartered, subsidiary bank.

* Pursuant to Rule 28.1, the petitioners state that the National Association of Professional Insurance Agents, only, has a parent company, subsidiary (other than wholly-owned), or affiliate. That subsidiary is Certified Professional Insurance Agent, Inc.



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OPINIONS BELOW

The decision of the court of appeals (Pet. App. A, pp. 1a to 19a, *infra*) is reported at 890 F.2d 1275 (2d Cir. 1989). The decision of the Board of Governors of the Federal Reserve System ("Board") (Pet. App. C, pp.

22a to 45a, *infra*) is reported at 75 Fed. Res. Bull. 388 (1989). The decision of the court of appeals in a related proceeding, *Independent Insurance Agents of America, Inc., et al. v. Board of Governors* is reported at 838 F.2d 627 (2d Cir. 1988) (Pet. App. E, pp. 47a to 63a, *infra*). The decision of the Board in a related proceeding is reported at 73 Fed. Res. Bull. 876 (1987) (Pet. App. G, pp. 67a to 82a, *infra*).

JURISDICTION

The decision of the court of appeals was issued on November 29, 1989. A timely motion for rehearing and suggestion for hearing in banc was denied on January 18, 1990 (Pet. App. D, p. 46a, *infra*). The jurisdiction of this Court rests on 28 U.S.C. § 1254(1).

STATUTES AND REGULATIONS INVOLVED

Section 1841(b) and 1843(a) & (c)(8) of Title 12, United States Code, and 12 C.F.R. §§ 225.1(c)(3), 225.2(d) & (l), and 225.21(a) are reproduced in Pet. App. H, pp. 83a to 90a, *infra*.

STATEMENT

This case will decide whether federally-regulated bank holding companies may avoid the severe constraints of the Bank Holding Company Act on their nonbanking activities simply by conducting those activities in state-chartered bank subsidiaries. That issue may sound arcane, but to the banking, insurance, real estate, and similarly-situated industries, it is a "long-simmering" and "major controversy in this country," App. A at 3a, that the Federal Reserve Board recognizes to be "important."¹ As one banking commentator remarked after the

¹ Opposition of Respondent Board of Governors of the Federal Reserve System to Petitioners' Motion for Stay of Mandate at 5, *Independent Insurance Agents of America, Inc., et al. v. Board of Governors*, No. 89-4030 (2d Cir.) (filed January 24, 1990). See also text at 8 *infra*.

appellate decision was rendered, “[f]rustrated . . . bank holding companies [can now] center [desired nonbanking] businesses in state-chartered affiliate banks.” *Merchants National to Resume Sale of Insurance at Its Banks*, American Banker, Dec. 1, 1989 at 1.

Merchants National Corporation (“Merchants”), a bank holding company, is regulated by the Federal Reserve Board pursuant to the Bank Holding Company Act of 1956 (“BHCA” or “Act”), as amended, 12 U.S.C. § 1841, *et seq.* The Act offers a format by which ownership of banks and nonbanks can be combined within a single corporate structure, that is, a bank or nonbank company may acquire both banking and nonbanking subsidiaries so long as the parent holding company and those subsidiaries conform to the constraints of the BHCA.

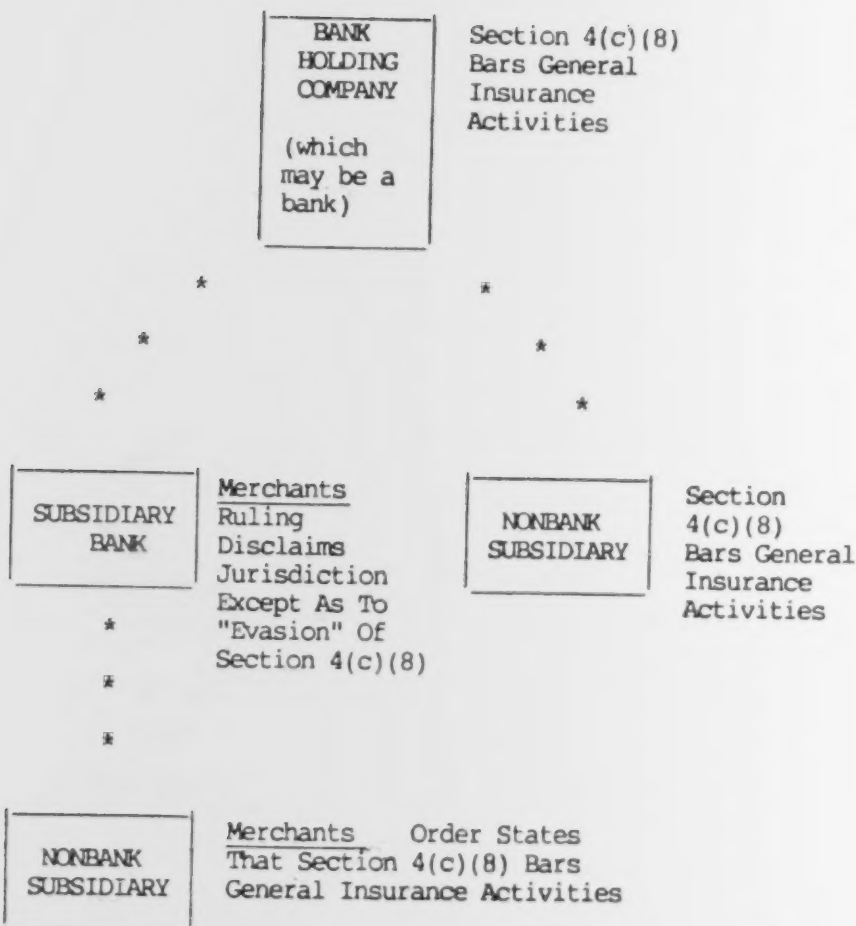
In 1986, Merchants applied to acquire two state-chartered banks in Indiana; one was selling insurance directly through bank employees and the other, Mid State Bank, owned an insurance agency. Several of the petitioners objected on the ground that Merchants’ ownership and operation of subsidiaries engaged in the sale of insurance would violate Section 4(c)(8) of the BHCA. That provision, in relevant part, states that bank holding companies may not “provide insurance as principal, agent, or broker.”

In 1989, the Federal Reserve Board approved Merchants’ assumption of the insurance activities. *See Merchants National Corporation*, 75 Fed. Res. Bull. 388 (1989) (App. C at 22a) (“*Merchants Order*”).² The

² Initially the Board had permitted Merchants to acquire the banks, but not their insurance activities. In 1987, the Board subsequently approved the acquisition of the insurance activities. *See Merchants National Corporation*, 73 Fed. Res. Bull. 876 (1987) (App. G at 67a). That order was reversed because its issuance violated a moratorium, then in effect, that prohibited the Federal Reserve Board from deciding this issue. *See Independent Insurance*

Board held that the nonbanking prohibitions of Section 4 generally do not apply to the direct activities of a subsidiary bank of a bank holding company. At the same time, the Board recognized that the insurance prohibition does apply if (i) the state bank is itself a bank holding company, (ii) the state bank subsidiary is being used to "evade" the purposes of the Act, or (iii) the state bank engages in insurance activities through its ownership of a separate nonbanking subsidiary. App. C at 28a, 41a. Thus, as the chart below depicts, the Board concluded that the nonbanking restrictions of Section 4(c)(8) are generally inapplicable so long as a bank holding company conducts its insurance activities inside a subsidiary bank, rather than through a nonbanking subsidiary. To thus avoid the application of Section 4(c)(8) to it, Merchants promised to dissolve the insurance agency owned by Mid State Bank and to move that business directly into the bank. App. C at 24a.

Prompt appellate review followed. See 12 U.S.C. § 1848. Over the Board's objection, the court granted a stay pending oral argument and, at oral argument, extended the stay pending decision. App. B at 20a, 21a.



When it reached the merits, the court commented critically on the Board's interpretation of the scope of Section 4:

Perhaps the most perplexing aspect of the structural arguments concerns the Board's contention that though it has no authority to preclude bank subsidiaries of a bank holding company from engaging in nonbank activities, it does have authority to preclude the subsidiaries of a bank subsidiary from engaging in nonbank activities. Thus, the Board adopts a generation-skipping approach: It may prohibit nonbank activities by bank holding companies and by their "grandchildren," i.e., the subsidiaries of their bank subsidiaries, but not by their bank

“children,” *i.e.*, the holding companies’ immediate bank subsidiaries.

App. A at 14a. The court further found that the Board’s interpretation (i) lacked “consistency,” *id.* at 15a, (ii) failed to comport with the sole identified purpose behind the enactment of the insurance prohibition in Section 4(c)(8), *id.* at 15a, and (iii) afforded no explanation for plain language in the statute, *id.* at 14a. Nonetheless, the court believed that it must defer to the Board’s “reasonable” interpretation because the express statutory language failed to state, in so many words, that conduct of the challenged activities in a subsidiary bank was subject to the insurance prohibition. App. A at 19a.³

REASONS FOR GRANTING THE WRIT

The ability of bank holding companies to enter non-banking businesses free from the constraints of the BHCA has enormous practical and legal consequences.

Congress has separated the banking industry from general commercial activities in order to preserve the stability of banking institutions and to protect nonbanking businesses from the unfair effects of bank competition. The BHCA expressly focuses on the need to limit the non-banking activities of holding companies, which can easily combine banking and nonbanking activities within a single corporate structure. But the ruling below enables bank holding companies to shrug off these constraints simply by conducting nonbanking activities directly within a subsidiary bank rather than through a nonbanking subsidiary of the holding company. Such intra-corporate maneuvering exposes the commercial banking industry to the same morass that has befallen the savings & loan industry, whose excesses will cost American tax-

³ The Second Circuit subsequently denied a petition for rehearing and a suggestion for hearing in banc. App. D at 46a. An Application for a Stay of Mandate of the U.S. Court of Appeals for the Second Circuit was denied by Justice Stevens on February 2, 1990.

payers billions of dollars. The entry of bank holding companies into nonbanking businesses ruled off-limits by Congress also threatens bank consumers—potential victims of credit coercion—and competing industries—put in competition with banking entities able to use the federal safety net and federal deposit insurance for their narrow competitive advantage.

These unprecedented, nationwide consequences flow from the Second Circuit's fundamental misreading of *Chevron U.S.A., Inc. v. Natural Resources Defense Council, Inc.*, 467 U.S. 837 (1984). The court, in common with other courts, failed to understand that no deference is due to an administrative interpretation until after a court fully analyzes congressional intent using all of the "traditional tools of statutory construction." *Id.* at 843 n.9. Rather, the court adopted a deferential standard of review immediately upon concluding that the express statutory language does not neatly answer the question presented to it.

Correct application of *Chevron* requires that the *Merchants* Order be struck down as inconsistent with the language and purpose of the BHCA. The insurance prohibition provides generally that it is not permissible for "a bank holding company to provide insurance as a principal, agent or broker," Section 4(c)(8), 12 U.S.C. § 1843 (c)(8); a prohibition that is designed to "implement a congressional policy against control of banking and non-banking enterprises by a single business entity." App. A at 10a (quoting *Lewis v. BT Investment Managers, Inc.*, 447 U.S. 27, 46 (1980)). Accordingly, the statute's insurance bar applies to every insurance activity in which a bank holding company may engage.

The lower courts' systematic abrogation of *Chevron*'s careful two-step analysis inevitably leads courts to accord unwarranted deference to administrative interpretation—a result that inevitably shifts power from Congress, whose intent has not been fully explored, to administrative

agencies, which have the later word. In an era of divided government particularly, that misuse of *Chevron* erodes basic principles of shared power among the branches of the federal government.

I. THE ABILITY OF BANK HOLDING COMPANIES TO ENTER NONBANKING BUSINESSES FREE FROM THE RESTRAINTS OF THE BANK HOLDING COMPANY ACT RAISES IMPORTANT, NATIONAL ISSUES THAT SHOULD BE RESOLVED BY THIS COURT

The *Merchants* Order holds that the BHCA does not generally limit the nonbanking activities of bank holding companies so long as the bank holding companies conduct those activities directly through a state-chartered subsidiary bank. As even the Board acknowledges, that issue raises “significant legal questions” involving “important and fundamental legal and policy issues.” *Board Statement on Applications to Acquire State-chartered Banks in South Dakota* at 1, 2 (Jan. 5, 1984). Indeed, the court below recognized that the *Merchants* Order contravenes the basic purpose of the BHCA: “‘to implement a congressional policy against control of banking and nonbanking enterprises by a single business entity.’” App. A at 10a (quoting *Lewis v. BT Investment Managers, Inc.*, 447 U.S. 27, 46 (1980)) ; *id.* at 15a.

The *Merchants* Order threatens immediate and nationwide consequences. Congress intended the nonbanking limitations of the Act to protect the financial stability of the nation’s banking system, S. Rep. No. 1095, 84th Cong., 1st Sess. 5 (1955), and to ensure that banking institutions cannot (i) abuse their role as impartial arbiters of credit, (ii) tie the provision of banking services, like loans, to the sale of nonbanking products, like insurance, and (iii) assume an unfair advantage over nonbanking competitors by virtue of their unique access to federally-insured funds. H.R. Rep. No. 609, 84th Cong., 1st Sess. 16 (1955); 115 Cong. Rec. 32894 (1969) (Chairman

Patman). In fact, the Board itself recently explained that the BHCA limits the ability of subsidiary banks to operate nonbanking businesses in order to ensure that (i) the risks of commercial activities are not underwritten by federal deposit insurance funds, and (ii) commercial competition is not distorted. 53 Fed. Reg. 48915, 48918 (Dec. 5, 1988).⁴

Without the application of the BHCA to all parts of a holding company system, the spread of nonbanking powers for bank holding companies will go far "beyond the academic or the episodic." *Rice v. Sioux City Memorial Park Cemetery, Inc.*, 349 U.S. 70, 74 (1955). A professional association of state bank regulators has concluded that a number of states are now in the business of granting nonbanking authority to their state-chartered banks that exceed the limits of the BHCA:

Insurance Underwriting (5 States)
 Insurance Brokerage (12 States)
 Real Estate Equity Participation (23 States)
 Real Estate Development (23 States)
 Real Estate Brokerage (6 States)
 Securities Underwriting (17 States)
 Securities Brokerage (21 States).⁵

State willingness to authorize nonbanking activities includes, in addition, the operation of an amusement park,

⁴ Consistent with these policies, the Board has ruled courier services off-limits to the subsidiary banks of bank holding companies, 12 C.F.R. § 225.129 (1973); 38 Fed. Reg. 32126 (Nov. 21, 1973), and this Court has affirmed the Board's power to restrict the manner in which bank subsidiary employees can be involved in the permissible activities of a securities affiliate. See *Board of Governors v. Investment Company Institute*, 450 U.S. 46, 59 n.25 (1981); 12 C.F.R. § 225.125(h) (1989).

⁵ Statement of James Gilleran on behalf of The Conference of State Bank Supervisors Before The House Subcommittee on Financial Institutions Supervision, Regulation and Insurance of the Committee on Banking, Finance and Urban Affairs of the House of Representatives, Attachment 2 (April 4, 1990).

see Federal Reserve Board Docket No. R-0652 (comments of New Jersey Bankers Ass'n) (letter of Jan. 27, 1989), and, in the thrift context, the ownership of windmill farms. See *Money Brokers Deserve Share of Blame For Thrift Woes*, *American Banker*, March 3, 1989 at 5. The Delaware State Senate is now considering a bill, passed by the House, designed to grant Citicorp and other large, money center bank holding companies the power to underwrite and sell insurance nationwide. *Insurers, Lawmakers Raise Concerns About Implications of Merchants National Ruling*, *Banking Report (BNA)* No. 14, at 611 (April 9, 1990).

The ability of bank holding companies to enter risky businesses directly threatens to compromise the financial stability of bank holding companies. One cause of the current S&L crisis was state willingness to permit their state-chartered institutions to engage in a wide variety of nonbanking activities, including, most notably, real estate investment. See *New Estimate on Savings Bailout Says Cost Could Be \$500 Billion*, *The New York Times*, April 7, 1990 at A1. The cost of resolving the S&L mess has escalated sharply; it is now estimated at one half a trillion dollars. *Id.* The risk to bank holding companies from real estate development and property & casualty insurance underwriting, to name but two examples, is too plain to be doubted. See also 52 Fed. Reg. 543, 544 (Jan. 7, 1987) (Board statement that real estate investment activity involves a "significant degree of risk").

Apart even from risk to their own stability, "there is little question that bank holding companies can and do provide the rawest form of unfair competition for small businessmen."⁶ Consumers of commercial services and products will face the fear and threat of banks tying the

⁶ Bank Holding Company Legislation and Related Issues: Hearings on H.R. 2255, H.R. 2427, H.R. 2856, H.R. 4004 Before the Subcommittee on Financial Institutions Supervision, Regulation and Insurance of the House Committee on Banking, Finance and Urban

availability of credit to the purchase of commercial products. Similarly, commercial competitors will confront (i) the loss of customers subjected to coercion or simply unwilling to risk the loss of their bank's credit, (ii) the loss of credit if they compete with banks that are both creditor and competitor, and (iii) the competitive disadvantage created by their bank competitors' access to cheap funds brought into the bank as a result of federal deposit insurance.

These concerns are not speculative. In 1969, the House Banking Committee heard testimony "concerning the kind of pressure banks have exerted to gain customers for various departments of the bank," and Congress was told "how banks can use their life and death power to grant or withhold credit to influence critical policy decisions of nonbanking corporations." 115 Cong. Rec. 32894 (1969) (statement of Chairman Patman). Within the past three weeks, the insurance commissioner of a state that permits insurance sales by its state-chartered banks told Congress that he personally has been subjected to bank coercion, despite federal and state anti-tying laws. J. Long, Testimony Before the Subcommittee on Financial Institutions Supervision, Regulation and Insurance of the House Committee on Banking, Finance and Urban Affairs (April 4, 1990).

The danger inherent in implementation of the Board Order is so patent that the Second Circuit twice stayed that order over the Board's objections. Large bank holding companies have taken advantage of the ruling to conduct activities declared impermissible by the Act. Just this month, for example, the nation's ninth largest bank holding company announced plans to sell insurance in 77 bank offices in California by the end of 1990. That action follows on the heels of "aggressive" insurance sales efforts already conducted in California by the nation's fifth

Affairs, 96th Cong., 1st Sess. 2 (1979) (remarks of Cong. St Germain).

largest bank holding company. See *First Interstate Targets Insurance*, American Banker, April 11, 1990 at 6; *Top 100 U.S. Bank Holding Companies*, American Banker, April 11, 1990 at 10, 12. Before the dangers threatened by the *Merchants Order* can come to full fruition, this Court should consider whether Congress intended these results.

II. THE SECOND CIRCUIT, IN COMMON WITH OTHER FEDERAL COURTS, FAILED TO APPRECIATE AND APPLY THE IMPORTANT PRINCIPLES OF *CHEVRON U.S.A., INC. v. NATURAL RESOURCES DEFENSE COUNCIL, INC.*

In *Chevron U.S.A., Inc. v. Natural Resources Defense Council, Inc.*, 467 U.S. 837 (1984), this Court enunciated the fundamental standards to guide judicial review of administrative decisions. *First*, a court must use "traditional tools of statutory construction," to determine "whether Congress has directly spoken to the precise question at issue." *Id.* at 842, 843 n.9. *Second*, and if "the statute is silent or ambiguous with respect to the specific issue," the court must determine whether the administrative agency has rendered a "permissible construction of the statute." *Id.* at 843; see *Sullivan v. Everhart*, 110 S.Ct. 960 (1990).

Each step has its own independent significance in ensuring the separation of powers. The first step ensures that original congressional intent receives the greatest deference and that close examination of legislative materials, including most obviously the language of the statute itself, precedes any attempt to ascertain how administrative agencies currently view the meaning or purpose of the law. Failure to follow legislative intent carefully would "usurp a power which our democracy has lodged in its elected legislature." F. Frankfurter, *Some Reflections on the Reading of Statutes*, 47 Col. L. Rev. 527, 534 (1947). The requirement that congressional intent be

carefully observed and fully vindicated is especially important in an era of divided government, when an administrative agency may be governed by appointees of one political party, and one or both of the houses of Congress controlled by another. Our federal system of government was designed, after all, to provide "a vigorous Legislative Branch and a separate and wholly independent Executive Branch" *Bowsher v. Synar*, 478 U.S. 714, 722 (1986).

Unfortunately, a number of courts, including the court below, have focused on step two to the detriment of step one. To be sure, an apt understanding of the judicial role mandates that courts not trench upon the legitimate function of an administrative agency. Disregard of the importance of step one, however, devalues the importance of congressional intent and subordinates the role of the legislative branch. Yet many courts, including the court below, believe that their authority under step one permits only a glancing look at the statute for a sentence that straightforwardly answers the question presented to the court by the litigants. But cases that easy seldom require the attention of the federal courts, and the federal courts, when they are called upon to decide issues of statutory interpretation, are "not to assay whether Congress might have stated that intent more naturally, more artfully, or more pithily." *Sullivan v. Everhart*, 110 S.Ct. at 973 (Stevens, J., dissenting).

The court below began and ended its independent review of congressional intent with the observation "We find no provision that says, in substance, 'The Board may not regulate the activities of bank subsidiaries of bank holding companies [or that says] 'Bank subsidiaries of bank holding companies may not engage in non-bank activities.'" App. A at 11a-12a. Without study of the express statutory language and congressional purpose, *id.*, the court then moved hastily to step two and pronounced the Board interpretation "permissible." That

failure to apply *Chevron* correctly proved to be outcome determinative. See Part III *infra*.

The court's error reflects a wide-spread difficulty in the lower courts. For example, in *Verna v. Coler*, 893 F.2d 1238 (11th Cir. 1990), the court adopted a *Chevron* analysis that, "[r]ather than beginning the analysis by determining whether Congress has clearly expressed its intent . . . proceeds to the second question and considers whether the agency's interpretation of the statute is reasonable." *Id.* at 1240 (Hatchett, J., dissenting). See also *Lile v. University of Iowa Hospitals and Clinics*, 886 F.2d 157, 160 (8th Cir. 1989) (deferring to an agency immediately upon finding that a statutory term, "governmental program," was ambiguous).

That problem has affected a number of other cases involving the Board. In *National Association of Casualty & Surety Agents v. Board of Governors*, 856 F.2d 282 (D.C. Cir. 1988), *reh'g en banc denied*, 862 F.2d 351, *cert. denied*, 109 S.Ct. 2430 (1989), even plain language was insufficient to prevent the court from analyzing the agency action under step two. In that case, the court asserted without explanation that an express statutory term "might be thought to be a fortuitous choice . . .", and went on to uphold an administrative interpretation even though the court "prefer[ed] petitioners' construction of the statute over the Board's." *Id.* at 288, 289; see *id.* at 291-92 (Buckley, J., dissenting) (the "language could hardly be more precise. . . . If a statute is unambiguous, as it is in this case, judicial inquiry is normally complete").⁷ Similarly, in *Securities Industry Ass'n*

⁷ In a concurrence to the appellate court's denial of rehearing en banc, the circuit judges representing the majority view explained, without modifying their earlier opinion, that they found the relevant statutory provision ambiguous, but continued to assert that "a myopic focus on Congress' selection of a definite or indefinite article could occasion results that . . . would be unexpected." *National Association of Casualty & Surety Agents v. Board of Governors*, 862 F.2d 351, 353 (D.C. Cir. 1988).

v. Board of Governors, 807 F.2d 1052, 1056 (D.C. Cir. 1986), the court moved to step two before examining the statute or other indicia of congressional intent. In order to safeguard principles of the separation of powers, this consistent misunderstanding of *Chevron* requires this Court's immediate attention.

III. THE NONBANKING LIMITATIONS OF THE BANK HOLDING COMPANY ACT APPLY TO ALL SUBSIDIARIES OF A BANK HOLDING COMPANY

The second issue raised by this petition is, of course, whether the *Merchants* Order comports with the requirements of the BHCA, which generally states that it is not permissible "for a bank holding company to provide insurance as a principal, agent, or broker" Section 4(c)(8), 12 U.S.C. § 1843(c)(8). For three basic reasons, the *Merchants* Order cannot survive close analysis.

First, the clear language of Section 4(a)(2) applies the nonbanking restrictions of Section 4(c)(8) whenever a bank holding company "engage[s] in any activities" not otherwise authorized by Section 4(a)(2). That extremely broad statutory language reaches every conceivable holding company act, including directing and profiting from a subsidiary bank's insurance activities. That conclusion is confirmed by Section 4(c)(8), which (i) sets forth the prohibition on insurance activities, (ii) is incorporated by reference into Section 4(a)(2), and (iii) as the lower court recognized, uses terms, here the words "company" and "affiliate," that include both banks and nonbanks.⁸

⁸ The court found the statutory language to be unclear largely because it accepted the Board's argument that petitioners' reading of the statutory language would override section 4(c)(14), which authorizes a bank holding company to own an export company. 12 U.S.C. § 1843(c)(14). These petitioners had explained, however, that the export provision falls within the express language of an exception to section 4(a)(2) that permits bank holding companies

Second, only the petitioners' interpretation comports with the acknowledged purpose of Section 4: "to implement a congressional policy against control of banking and nonbanking enterprises by a single business entity." App. A at 10a (quoting *Lewis v. BT Investment Managers, Inc.*, 447 U.S. 27, 46 (1980)). That was obvious to the lower court, which described the Board's approach as "perplexing," noted the "apparent awkwardness and perhaps illogic," of the Board's view, and expressed "wonder" at the effect of the Board's interpretation. App. A at 15a. By contrast, the petitioners' "position has the virtue of consistency in reading the Act to preclude nonbank activities throughout a bank holding company's system." *Id.*

The lower court ultimately concluded, however, that Congress may have "adjusted the competing positions of strong forces with a compromise of imperfect symmetry." *Id.* That justification for the Board order, however, bases deference on mere speculation; neither the Court nor the Board relied upon any "competing position" that may have forced a legislative "compromise." The lower court's reliance on this Court's analysis in *Board of Governors v. Dimension Financial Corp.*, 474 U.S. 361, 374 (1986), see App. A at 15a, was thus inapposite.⁹

to manage and control all subsidiaries "authorized under this Act." 12 U.S.C. § 1843(a)(2)(A). That which is authorized by section 4(c)(14) is, therefore, permissible under Section 4(a)(2). The insurance activities at issue here are not only not authorized, they are forbidden by the Act.

⁹ In the *Dimension Financial* case, this Court reversed a Board interpretation that violated the plain language of the Act, even though it arguably furthered a legislative purpose. Unlike that case, here the petitioners do not invoke the "'plain purpose' of legislation at the expense of the terms of the statute itself." 474 U.S. at 374. Rather, the Board's interpretation conflicts with both the plain language and the express legislative purpose.

Third, the competing Board view cannot be squared with any statutory language or congressional intent. The Board does not contend that all state-chartered banks or all entities regulated by state banking authorities lie beyond its jurisdiction. To the contrary, the Board acknowledged that the nonbanking limitations apply if (i) a state-chartered bank is itself a parent bank holding company, (ii) a state-chartered bank is being used to “evade” the purposes of the Act, *see Citicorp (South Dakota)*, 71 Fed. Res. Bull. 789 (1985), or (iii) the nonbanking activities are being conducted in a nonbanking subsidiary of a state-chartered subsidiary bank. There is no evidence, and the Board supplied none, to support the view that Congress wished the insurance prohibition of Section 4(c)(8) to apply to entities subject to state banking regulation only some of the time. That the nonbanking limitations of the BHCA overlap—in at least these three, Board-acknowledged circumstances—with state banking regulation further demonstrates that exclusive state control of state-regulated entities was not a purpose of the Act. To take but one example, the Board supplied no indicia of statutory intent to support the view that Congress intended the insurance prohibition to apply only when the Board concluded that a state-chartered bank was being used to “evade” the BHCA and not when, as in this case, insurance activities are moved into a state-chartered bank expressly to avoid application of the Act.

The failure of the Board to advance a consistent view of the statutory structure as a whole weighs heavily against adoption of its analysis. *United Housing Foundation, Inc. v. Forman*, 421 U.S. 837, 858 n.25 (1975). Thus, as former Board Governor Rice concluded, “the terms, structure, legislative history and purpose of the Act make clear that a bank holding company may not avoid the nonbanking restrictions of the Act by conducting these activities through a subsidiary bank”. *Citicorp (South*

Dakota), 71 Fed. Res. Bull. 789, 792 (1985) (Rice, concurring).¹⁰

CONCLUSION

For the reasons stated herein, the petitioners respectfully request that the petition for a writ of certiorari be granted.

Respectfully submitted,

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April 18, 1990

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¹⁰ The court below derived some comfort from this Court's decision in *Board of Governors v. Investment Company Institute*, 450 U.S. 46, 59 n.25 (1981), which states, in part, that the "authority of . . . state member banks to furnish investment advisory services does not derive from the Board's regulation," but rather, that its scope "is to be determined by a particular bank's primary supervisory agency." App. A at 18a. The lower court failed to recognize, however, that the quoted footnote goes on to uphold the "imposition of restrictions on banks [that] prevented bank holding companies and their nonbanking subsidiaries from evading the restrictions by allowing the subsidiary banks to perform the restricted activities." *Id.*; see n.4 *supra*. That sort of evasion is exactly what is at issue here.

APPENDICES



APPENDIX A

UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT

No. 1243—August Term 1988

Argued: June 1, 1989

Decided: November 29, 1989

Docket No. 89-4030

INDEPENDENT INSURANCE AGENTS OF AMERICA, INC.,
INDEPENDENT INSURANCE AGENTS OF NEW YORK, INC.,
NEW YORK STATE ASSOC. OF LIFE UNDERWRITERS, AND
PROFESSIONAL INSURANCE AGENTS OF NEW YORK, INC.,
Petitioners,

—v.—

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM,
Respondent,

MERCHANTS NATIONAL CORPORATION, THE NATIONAL ASSOCIATION OF CASUALTY AND SURETY AGENTS, THE NATIONAL ASSOCIATION OF LIFE UNDERWRITERS, THE NATIONAL ASSOCIATION OF PROFESSIONAL INSURANCE AGENTS, AND THE NATIONAL ASSOCIATION OF SURETY BOND PRODUCERS,
Intervenors.

Before:

KAUFMAN, NEWMAN, and MINER,
Circuit Judges.

Petition for review of an order of the Federal Reserve Board permitting two bank subsidiaries of a bank holding company to sell insurance.

Petition denied.

JONATHAN B. SALLET, Wash., D.C. (Jay L. Alexander, Lisa D. Burget, Miller, Cassidy, Larroca & Lewin, Wash., D.C., on the brief), *for petitioners and insurance-agent intervenors.*

DOUGLAS B. JORDAN, Senior Atty., Board of Governors of Fed. Reserve System, Wash., D.C. (John R. Bolton, Asst. Atty. Gen., U.S. Dept. of Justice; J. Virgil Mattingly, Gen. Counsel, Richard M. Ashton, Assoc. Gen. Counsel, Board of Governors of Fed. Reserve System, Wash., D.C., on the brief), *for respondent.*

JAMES A. McDERMOTT, Indianapolis, Ind. (Stanley C. Fickle, Barnes & Thornburg, Indianapolis, Ind., on the brief), *for intervenor Merchants National Corp.*

(Paul B. Galvani, Martin E. Lybecker, William L. Patton, Alan G. Priest, Mark P. Szpak, Ropes & Gray, Wash., D.C.; Laurene K. Janik, Natl. Ass'n of Realtors, Chicago, Ill., *submitted a brief for amici curiae Insurance Company Associations and National Association of Realtors.*)

(Robert M. Kurucza, Robert G. Ballen, Steven S. Rosenthal, Debra L. Lagapa, Leslie J. Cloutier, Morrison & Foerster, Wash., D.C., *submitted a brief for amicus curiae California Bankers Clearing House Association.*)

(Ernest Gellhorn, Robert C. Jones, Jones, Day, Reavis & Pogue, Wash., D.C., *submitted a brief for amici curiae Conference of State Bank Supervisors, Independent Bankers Ass'n of America, and National Council of Savings Institutions.*)

(John J. Gill, Michael F. Crotty, American Bankers Ass'n, Wash., D.C.; James T. McIntyre, Jr., Randi S.

Field, McNair Law Firm, Wash., D.C.; Richard Whiting, Ass'n of Bank Holding Companies, Wash., D.C.; Charles L. Marinaccio, Kelley, Drye & Warren, Wash., D.C., *submitted a brief for amici curiae American Bankers Association, Association of Bank Holding Companies, Insurance/Financial Affiliates of America, and Association of Reserve City Bankers.*)

(Linley E. Pearson, Atty. Gen., Samuel L. Bolinger, Deputy Atty. Gen., Indianapolis, Ind., *submitted a brief for amicus curiae Indiana Department of Financial Institutions.*)

JON O. NEWMAN, *Circuit Judge:*

The extent to which banks should be permitted to engage in nonbanking activities is a major controversy in this country, attracting the increasing attention of Congress, administrative agencies, and courts. This petition for review of an order of the Board of Governors of the Federal Reserve System ("the Board" or "the Fed") brings before us one facet of that controversy. The issue is whether the Fed was entitled to conclude that section 4 of the Bank Holding Company Act of 1956 ("the Act" or "BHCA") does not restrict bank subsidiaries of a bank holding company from selling insurance. The issue arises on a petition filed by the Independent Insurance Agents of American ("IIAA") challenging the Board's March 3, 1989, order, which permitted two Indiana state banks acquired by the Merchants National Corporation, a bank holding company, to resume specified insurance activities permitted under Indiana law. *Merchants National Corp.*, 75 Fed. Res. Bull. 388 (1989) ("*Merchants II*"). The Board's order rested upon a determination that the nonbanking prohibitions of section 4 of the Act, as amended, 12 U.S.C. § 1843 (1988), do not apply to the activities of the bank subsidiaries of a bank holding company. Concluding that this construction of section 4 is within the

range of reasonable interpretation that the pertinent administrative agency is entitled to make, we deny the petition for review and leave this long-simmering controversy for such further consideration as Congress cares to give it.

Background

Litigation history. This matter is before this Court for the second time. On the prior occasion, we granted IIAA's petition for review after concluding, contrary to the Board's prior decision in this matter, *Merchants National Corp.*, 73 Fed. Res. Bull. 876 (1987) ("*Merchants I*"), that the Board's authority to permit insurance activities by the bank subsidiaries of Merchants National was temporarily precluded by the moratorium provisions of the Competitive Equality Banking Act of 1987 ("CEBA"), Pub. L. No. 100-86, 101 Stat. 552 (1987), reprinted in 12 U.S.C. § 1841 note (1988). See *Independent Insurance Agents of America, Inc. v. Board of Governors*, 838 F.2d 627, 633-34 (2d Cir. 1988). The moratorium, which was effective from March 6, 1987, to March 1, 1988, prohibited the Fed from issuing any order "that would have the effect of increasing the insurance powers" of a bank holding company or its banking or nonbanking subsidiaries. CEBA § 201(b)(3).

In anticipation of the expiration of the moratorium, Merchants National renewed its request that the Board authorize its Indiana banking subsidiaries to engage in insurance activities. After providing notice of this request, 52 Fed. Reg. 8966 (1987), and assessing the comments that were received, the Board issued the order that is the subject of the pending petition for review. This Court granted a stay of the order pending oral argument and continued the stay pending decision.

The statutory framework. Before introducing the facts, it will be helpful to outline briefly the pertinent statutory provisions of the Bank Holding Company Act.

The principal regulatory powers of the Fed concerning bank holding companies are set forth in sections 3 and 4 of the Act. 12 U.S.C. §§ 1842, 1843. Section 3 requires Board approval of the acquisition of ownership or control of any bank by a bank holding company, with narrow exceptions not here relevant. Section 3 sets forth factors governing acquisition approval, focusing on the competitive effect of the proposed acquisition, the financial and managerial resources of both the holding company and the acquired bank, and the convenience and needs of the community served. 12 U.S.C. § 1842(c).

Section 4 of the Act, the focal point of the Board's order in this case, contains two sets of prohibitions. First, it specifies, in what might be called the "ownership clause," that a bank holding company may not "retain direct or indirect ownership or control of any voting shares of any company which is not a bank or bank holding company." 12 U.S.C. § 1843(a)(2). Second, it provides, in what might be called the "activities clause," that a bank holding company may not "engage in any activities other than (A) those of banking or of managing or controlling banks . . . and (B) those permitted under [section 4(c)(8) of the Act]" *Id.* Section 4(c)(8) sets forth the so-called "closely related to banking" exception to the nonbanking provision. *Id.* § 1843(c)(8). In relevant part, section 4(c)(8) states that the section 4(a) nonbanking prohibitions shall not bar ownership by a bank holding company of:

shares of any company the activities of which the Board after due notice and opportunity for hearing has determined (by order or regulation) to be so closely related to banking or managing or controlling banks as to be a proper incident thereto, but for purposes of this subsection it is not closely related to banking or managing or controlling banks for a bank holding company to provide insurance as a principal, agent or broker

Id.

Facts. A number of states, including Indiana,¹ historically have authorized state-chartered banks to provide insurance services to their customers. On July 1, 1986, Merchants National Corporation, a bank holding company within the meaning of the BHCA, 12 U.S.C. § 1841(a), sought permission from the Fed to acquire the stock of two banks chartered under the laws of the State of Indiana, the Anderson Banking Company ("Anderson Bank") and the Mid State Bank of Hendricks County ("Mid State Bank"). Both of these state banks had engaged in general insurance activities prior to the date of Merchants National's applications, Anderson Bank directly since its incorporation in 1916, and Mid State Bank since its purchase of an insurance agency in 1985. Merchants National subsequently made a commitment that Mid State Bank would transfer to itself all insurance activities from its insurance agency subsidiary and thereafter conduct all such activities directly in the bank.

The initial Merchants National applications were protested by various insurance industry trade groups, including the IIAA, on the ground that the provisions of section 4 of the Act apply to the insurance activities of state banks owned by bank holding companies and therefore that the acquisitions of Anderson Bank and Mid State Bank could not be approved without termination of their insurance activities to the extent required under section 4. In response to the protests, Merchants National committed that it would cause the banks to divest their insurance agency activities within two years unless, within that time, it received Board approval for the banks to retain their insurance activities. Merchants National agreed that, prior to such approval, the banks would limit their insurance activities to the renewal of

¹ Ind. Code § 28-1-11-2 provides: "Any bank or trust company shall have power . . . to solicit and write insurance as agent or broker for any insurance company authorized to do business in this state, other than a life insurance company."

existing policies. In light of these commitments, the Board approved the applications on October 29, 1986. 72 Fed. Res. Bull. 838 (1986).

On February 5, 1987, Merchants National filed an application seeking Board approval for Anderson Bank and Mid State Bank to resume the insurance activities that had just been suspended pursuant to the acquisition commitments. Merchants National sought permission on two alternative grounds. First, it contended that Anderson Bank and Mid State Bank were exempt from the insurance provisions of section 4 of the Act pursuant to the "grandfather" provision of section 4(c)(8)(D), as amended, 12 U.S.C. § 1843(c)(8)(D), under which a bank holding company or any of its subsidiaries is permitted to engage in insurance agency activity in which the holding company or the subsidiary was engaged on May 1, 1982, subject to certain geographical and functional limitations. Second, Merchants National sought more broadly a determination that the nonbanking prohibitions of section 4 of the Act do not apply to activities conducted directly by banking subsidiaries of a bank holding company. In *Merchants I*, the Board rejected the first contention but agreed with the second one. After the prior appeal to this Court and the expiration of the moratorium, the Board issued the decision challenged on this petition for review. *Merchants II*.

The Board's Decision

The core of the Board's decision in *Merchants II* was its conclusion, previously expressed in *Merchants I*, that the provisions of section 4 limiting the nonbanking activities of bank holding companies do not apply to bank subsidiaries of a bank holding company. Consistent with this view, the Board also ruled, as it had in *Merchants I*, that section 4's prohibition upon a bank holding company's acquisition of a nonbanking entity (unless that entity engages only in activities "closely related to bank-

ing") does not apply to a holding company's acquisition of a bank. The Board recognized an exception to this latter conclusion in those instances, illustrated by the *Citicorp (South Dakota)* case, 71 Fed. Res. Bull. 789 (1985), where the Board finds an evasion arising from a holding company's acquisition of an entity that purports to be a "bank" but engages in insignificant banking activities, indicating that the acquisition is "primarily, if not solely" for the purpose of enabling the holding company to engage in the target's nonbanking activities.² *Merchants II*, Fed. Res. slip op. at 8 n.11.

The Board grounded its conclusions on several considerations. First, the Board pointed out that the limitations of section 4(a)(2) apply in express terms to "bank holding companies," not to "banks." *Id.* at 11. Second, the Board relied on what it considered a structural argument: the "ownership clause" of section 4 restricts the entities that a bank holding company may acquire or retain, and the "activities clause" restricts the activities that the bank holding company itself may engage in. In the Board's view, if the restriction on activities applied to the activities of subsidiaries of a bank holding company, the restriction on acquisition or retention of non-bank entities would be superfluous. *Id.* at 11-13. Third, the Board emphasized that the restriction on acquisition or retention was broadly phrased to prohibit "direct or indirect" ownership, whereas the restriction on engaging in activities omitted the comparable adverbs "directly or indirectly," words the Board appears to acknowledge would have made the restrictions of section 4 applicable

² The Board decided *Citicorp* in the exercise of its authority under section 5 of the Act, 12 U.S.C. § 1844. The Supreme Court subsequently ruled that section 5 "only permits the Board to police within the boundaries of the Act." *Board of Governors v. Dimension Financial Corp.*, 474 U.S. 361, 373 n.6 (1986). We do not decide whether, in light of *Dimension Financial*, *Citicorp* was a proper exercise of the Commission's authority under section 5 or any other provision of the Act.

to activities of a bank holding company's subsidiaries. *Id.* at 12-13. Fourth, the Board asserted that since the enactment of the Bank Holding Company Act, it has consistently declined to read the activities restriction of section 4 as applicable to bank subsidiaries of a bank holding company. *Id.* at 15-16. Fifth, the Board found in the legislative history of the Bank Holding Company Act and its subsequent amendments a congressional purpose to leave the scope of permissible activities of bank subsidiaries of a bank holding company subject only to the authority that issued the banks' charter, without any further restriction for the Act itself.³ *Id.* at 17-20.

The Board also reckoned with and rejected an argument based on section 101(d) of CEBA, which amends section 3 of BHCA to permit qualified state-chartered savings banks to engage in any activity permitted by state law, but prohibits such banks from violating the insurance restrictions of section 4(c)(8). 12 U.S.C.

³ Though concluding that the provisions of section 4 do not apply to bank subsidiaries of a holding company, the Board somewhat inconsistently also concluded, as it had in *Merchants I*, that neither Anderson Bank nor Mid State Bank qualifies under the grandfather provision of the Garn-St. Germain Act, which is section 4(c)(8)(D) of the Bank Holding Company Act. The Board pointed out that Anderson Bank did not become a subsidiary of a bank holding company and Mid State Bank did not start selling insurance until after the May 1, 1982, grandfather date. If, as the Board concluded, section 4 is inapplicable to bank subsidiaries of a bank holding company, it is not readily apparent why the grandfather clause of section 4(c)(8) was inapplicable on the narrow ground that its precise terms were not met, rather than the broader ground that section 4, to which the clause is an exception, has no application to banking subsidiaries. Indeed, it is the Board's position that "the Garn-St. Germain Act has no applicability to situations . . . where the nonbanking provisions of section 4 of the [Bank Holding Company] Act do not apply." *Merchants II*, Fed. Res. slip op. at 8 n.10. Perhaps the Board simply felt it prudent to reckon with the first of Merchant National's alternative arguments and reject it on a narrow ground before proceeding to the second argument, which presented the broader ground.

§ 1842(f). It was contended that if section 4 did not restrict the nonbanking activities of bank subsidiaries of a bank holding company, an exemption for savings banks would not have been necessary. The Board responded that this amendment may have been adopted to confirm the Board's view in the face of arguments advanced by insurance trade associations and to provide special limitations applicable only to savings bank subsidiaries of a bank holding company. In this connection, the Board emphasized that Congress had considered and declined to enact legislation to extend the restrictions on savings bank subsidiaries to all bank subsidiaries of a bank holding company. *Merchants II*, Fed. Res. slip op. at 23-24; see H.R. Conf. Rep. No. 261, 100th Cong., 1st Sess. 130 (1987); S. Rep. No. 19, 100th Cong., 1st Sess. 33 (1987).

Finally, the Board noted that its decision leaving the activities of bank subsidiaries to regulation by the chartering authority applied only to activities carried on directly by those banks and did not insulate from section 4 the activities ~~of subsidiaries of the bank subsidiaries~~. This application of section 4 to third generation entities, those owned by the subsidiaries of a bank holding company, was based on section 2(g)(1) of the Act, 12 U.S.C. § 1841(g)(1), which provides that shares of such third generation entities are deemed to be held indirectly by the bank holding company; as a result, whether such entities may be owned by a subsidiary of a bank holding company is governed, in the Board's view, by section 4's limitation on entities that may be owned by a bank holding company. *Merchants II*, Fed. Res. slip op. at 25.

Discussion

There can be no doubt that the Bank Holding Company Act is "intended to implement a congressional policy against control of banking and nonbanking enterprises by a single business entity." See *Lewis v. BT Invest-*

ment Managers, Inc., 447 U.S. 27, 46 (1980). What is less clear is the extent to which Congress has decided to implement that policy. IIAA contends that Congress has required a nearly complete separation of banking and nonbanking activities, precluding bank holding companies and all entities within their systems from engaging in nonbanking activities other than the "closely related to banking" activities specifically identified in section 4(c)(8) of the Act. The Board believes that Congress has not gone so far. In its view, Congress required a significant degree of separation with respect to bank holding companies themselves, but did not wish to displace the traditional authority of state and national bank chartering authorities to determine what nonbanking activities could appropriately be engaged in by banks that are subject to their jurisdiction, even though such banks were owned by a bank holding company under the jurisdiction of the Fed.

In resolving this dispute, we must keep in mind that we are not making an initial construction of a statute, but rather reviewing a construction made by an expert regulatory agency. In that context, our task is to determine whether Congress has "directly spoken to the precise question at issue," and, if so, to give effect to any "unambiguously expressed intent of Congress," or, if not, to determine "whether the agency's answer is based on a permissible construction of the statute." *Chevron U.S.A., Inc. v. Natural Resources Defense Council, Inc.*, 467 U.S. 837, 842-43 (1984). Though both sides support their views of the statute by relying on some of the statutory language, we cannot say that the provisions of the Act reveal an unambiguous congressional intent concerning the precise question at issue. We find no provision that says, in substance, "The Board may not regulate the activities of bank subsidiaries of bank holding companies," or "Bank subsidiaries of bank holding companies may engage in nonbank activities to the extent permitted

by their chartering authorities." The Board reads the Act as if it contained such language. On the other hand, we find no provision that says, in substance, "Bank subsidiaries of bank holding companies may not engage in nonbank activities." The IIAA reads the Act as if it contained this wording. The question for us is whether the Board's interpretation of the language that does appear in the Act is reasonable, an inquiry we undertake by examining all relevant sources, including such clues as the statutory language may provide.

Both sides claim that the text of the Act supports their interpretations, and each can find some, but not overwhelming, support in various words and phrases. As the Board noted in its decision, the limitations of section 4(a)(2) apply in terms to "bank holding companies," not to "banks." However, that observation somewhat begs the question, which is whether the limitations upon bank holding companies should be interpreted to restrict the activities those entities may engage in *indirectly* through their banking subsidiaries. Of similarly little, if any weight, is the argument that because the "ownership clause" of section 4(a)(2) does not bar a bank holding company from owning subsidiary banks, the "activities clause" should be interpreted not to apply to activities of subsidiary banks. The argument is a *non sequitur*. It would be entirely sensible for Congress, if it wished, to bar a bank holding company from owning nonbanks and also prohibit a bank holding company from engaging indirectly in nonbank activities conducted by its bank subsidiaries. For its part, the IIAA points to the language prohibiting bank holding companies from engaging in nonbank activities and assumes that this language means "engage in directly or through subsidiaries."

Somewhat more supportive of the Board's position are textual arguments arising from comparisons of the "activities clause" with other language in section 4(a)(2). First, the grandfather proviso of section 4(a)(2)

permits a bank holding company to engage in those activities "in which directly or through a subsidiary" it was engaged in at designated times and under designated circumstances. The Board points out that no similar phrase modifies the "activities clause." Second, the "ownership clause" prohibits the retention of "direct or indirect" ownership of nonbanks, and no similar phrase modifies the prohibition on engaging in nonbank activities. The use of these phrases in section 4(a)(2) and their absence from the "activities clause" might imply a deliberate congressional choice not to restrict the activities of bank subsidiaries, *cf. Russell v. United States*, 464 U.S. 16, 23 (1983) (significance of different wording in statute), but might also result from drafting different clauses at different times and assembling them without intending differences in phrasing to have significance.

The Board derives a somewhat stronger argument for its interpretation from the structure of the Act. It points out that if the "activities clause" applied to subsidiaries of a bank holding company, the "ownership clause" would be virtually superfluous, since, under that reading, the "activities clause" alone would preclude a bank holding company from owning a nonbank. Moreover, as the Board further points out, such a reading would appear to create some internal inconsistencies. For example, section 4(c)(14) permits a bank holding company, under specified circumstances, to own an export trading company; however, this would be prohibited if the "activities clause" applied to subsidiaries of a bank holding company since that clause exempts only the "closely related to banking" activities set forth in section 4(c)(8), which do not include export trading. IIAA's only response is that the (c)(14) exemption would control over the (a)(2) "activities clause" since it comes later in the statute. *See Lodge 1858 v. Webb*, 580 F.2d 496, 510 (D.C. Cir.), *cert. denied*, 439 U.S. 927 (1978). That canon of construction may sometimes be helpful in resolving irrecon-

cilable inconsistencies, but it need not be invoked where the statute may be interpreted to avoid the inconsistency in the first place.

However, IIAA also finds support for its interpretation in the structure of section 4. As IIAA points out, section 4(c)(8), establishing the circumstances for exempting various entities from the restrictions of section 4, including the "activities clause" of section 4(a)(2), uses the term "company" to describe those entities, and "company" is defined by section 2(b) broadly enough to include a bank. *See* 12 U.S.C. § 1841(b). Moreover, section 4(c)(8) instructs the Board, in deciding whether a particular activity is "a proper incident to banking," to assess whether the performance of that activity "by an affiliate of a holding company" will produce public benefits, and "affiliate" is defined by section 2(k) to include a "company" and, hence, a bank. *See* 12 U.S.C. § 1841(k). The available inference is that subsidiary banks are subject to the "activities clause" because they are within the category of entities exempted from that clause by section 4(c)(8).

Perhaps the most perplexing aspect of the structural arguments concerns the Board's contention that though it has no authority to preclude bank subsidiaries of a bank holding company from engaging in nonbank activities, it does have authority to preclude the subsidiaries of a bank subsidiary from engaging in nonbank activities. Thus, the Board adopts a generation-skipping approach: It may prohibit nonbank activities by bank holding companies and by their "grandchildren," *i.e.*, the subsidiaries of their bank subsidiaries, but not by their bank "children," *i.e.*, the holding companies' immediate bank subsidiaries. The Board's rationale is that the prohibition in the "ownership clause" on "direct or indirect" ownership of nonbank entities precludes a bank holding company from indirectly owning the nonbank subsidiary of its own bank subsidiary.

This contention elicits conflicting responses from IIAA and Merchants National. IIAA contends that the Fed can prohibit nonbanking activities at all three levels and cites the apparent awkwardness and perhaps illogic of the Board's generation-skipping approach as evidence that the Board's interpretation of the "activities clause" is incorrect. As IIAA points out, under the Board's reading of section 4(a)(2), a holding company's bank subsidiary that owns a nonbank subsidiary can escape the prohibition of the "ownership clause" by merging the "grandchild" into the bank subsidiary and operating the nonbank activities itself. That is precisely what Mid-State Bank did in this proceeding. For its part, Merchants National argues that the Fed may bar nonbanking activities only of a holding company itself and may not preclude those of either second generation bank subsidiaries or their third generation subsidiaries.

IIAA's position has the virtue of consistency in reading the Act to preclude nonbank activities throughout a bank holding company's system. Moreover, if the Board is correct that Congress wished to leave the activities of bank subsidiaries subject to the regulation of only their chartering authorities, one is left to wonder why those authorities were not relied on to control all of a bank subsidiary's activities, whether conducted directly by the bank subsidiary itself or indirectly through its own subsidiary. On the other hand, if the Board is right that the Act leaves the nonbank activities of bank subsidiaries within the control of bank chartering authorities but precludes nonbank activities by holding companies and by the subsidiaries of their bank subsidiaries, this would not be the first time that Congress has adjusted the competing positions of strong forces with a compromise of imperfect symmetry. See *Board of Governors v. Dimension Financial Corp.*, 474 U.S. 361, 374 (1986). We think it prudent not to resolve the issue of the Board's authority over the nonbank activities of subsidiaries of bank subsidiaries until that issue is squarely presented.

IIAA endeavors to support its interpretation of the "activities clause" with isolated quotations from the legislative history of the Act. Some members of Congress expressed the view that the Act was intended to keep "banks" out of nonbank activities. As Congressman O'Hara put it, "I do not think, however, that any of my colleagues will question the soundness of the rule that banks should stick exclusively to banking and should be as free of nonbanking interests as C[æ]sar's wife from suspicion." 101 Cong. Rec. 8033 (1955). *See also* 102 Cong. Rec. 6853 (1956) (statement of Sen. Barkley); 101 Cong. Rec. 8030 (1955) (statement of Rep. Rains); *id.* at 8035 (statement of Rep. Multer); *id.* at 8184 (statement of Rep. Smith).

These remarks do not provide unambiguous support for IIAA's interpretation for several reasons. First, in some instances, it is not clear if the legislator is referring to bank subsidiaries of bank holding companies or to the holding companies themselves. Second, many expressions condemning nonbank activities, including one that explicitly mentions banks and bank holding companies, *see* 102 Cong. Rec. 6853 (1956) (statement of Sen. Barkley), focus on ownership interests, rather than the business activities that a bank subsidiary may conduct. Plainly, as the "ownership clause" commands, Congress did not want bank holding companies to own nonbanks. The legislative history, however, is remarkably free of clear statements indicating disapproval of nonbanking activities engaged in directly by bank subsidiaries. If such were the intent of Congress, one would expect to find a clear statement of such purpose in the key House and Senate reports. Finally, during the hearings the attention of Congress was specifically called to the range of activities that state chartering authorities were permitting for bank subsidiaries of bank holding companies, *see Control and Regulation of Bank Holding Companies: Hearings on H.R. 2674 Before the House Comm. on Banking and Currency*, 84th Cong., 1st Sess. 536, 553 (1955) (testi-

mony of Ellery C. Huntington), and some Congressmen expressed the view that the holding company bill would not modify such state regulatory authority, *id.* at 553 (statements of Rep. Spence and Rep. Brown).

Subsequent legislative forays into the field, though an uncertain source of prior congressional intent at best, *see Russello v. United States*, 464 U.S. at 26, reveal primarily that Congress finds this a difficult area in which to provide clear answers. In connection with the 1970 amendments to the Act, the House Committee on Banking and Currency reported a bill that, among other things, explicitly excluded insurance activities from the "closely related to banking" activities permitted under section 4(c)(8). H.R. Rep. No. 387, 91st Cong., 1st Sess. 9 (1969). Referring to the effect of this and another prohibition concerning sale of mutual funds, the Committee stated:

It should be emphasized that these two prohibitions apply only to the bank holding company and its non-banking subsidiaries and not to the bank subsidiaries of bank holding companies whose insurance agency and mutual fund operations are governed by other Federal and State laws. This is in keeping with the original concept of the 1956 act, which was to regulate bank holding companies and not subsidiary banks.

Id. at 15. The House then went further and amended the bill to identify a list of activities explicitly prohibited both to bank holding companies and all of their subsidiaries, including banks. 115 Cong. Rec. 33133-35. The Senate disagreed with this approach, *see* S. Rep. No. 1084, 91st Cong., 2d Sess. 12-16 (1970), and it was rejected in conference. H.R. Conf. Rep. No. 1447, 91st Cong., 2d Sess. 13-16 (1970).

Finally with respect to subsequent legislative attention, some significance must be attached to the fact that Con-

gress specifically called to its own attention the correctness of the Board's interpretation of the "activities clause" in *Merchants I* by enacting the moratorium provisions of CEBA and providing itself with a one-year opportunity to determine whether to legislate contrary to the Board's view. The moratorium expired without the passage of new legislation on this subject.

Case law has not directly focused on the issue now before us, but two decisions provide the Board with some comfort. When investment companies challenged the Board's determination that the services of an investment adviser to a closed-end investment company were "closely related to banking" under section 4(c)(8), they argued that the Board was allowing subsidiary banks to render such services. See *Board of Governors v. Investment Company Institute*, 450 U.S. 46, 59 n.25 (1981). The Supreme Court disagreed and noted with apparent approval the Board's view that whether such services could be rendered by subsidiary banks depended solely on the decisions of their chartering authorities:

The simple answer to this argument is that not only does the interpretive ruling confer no authorization to undertake any activities, but also the Board does not have the power to confer such authorization on banks. As the Board's opinion in this case stated:

"[T]he Board's regulation . . . authorizes investment advisory activity to be conducted by a nonbanking subsidiary of the holding company. The authority of national banks or state member banks to furnish investment advisory services does not derive from the Board's regulation; such authority would exist independently of the Board's regulation and its scope is to be determined by a particular bank's primary supervisory agency."

Id. Tilting in the same direction is *Cameron Financial Corp. v. Board of Governors*, 497 F.2d 841, 848 (4th Cir.

1974), which ruled that a bank subsidiary is not included within the term "subsidiary" for purposes of the grandfather provisions of section 4(a).

After assessing all of the relevant considerations, we are satisfied that the Board, acting within its sphere of competence, has made a reasonable interpretation of section 4(a)(2), one that confides decisions concerning the scope of insurance and other nonbank activities of bank subsidiaries to their national and state chartering authorities. If that interpretation is to be altered, Congress will have to enact suitable legislation.

The petition for review is denied.

APPENDIX B

UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT

At a stated Term of the United States Court of Appeals for the Second Circuit, held at the United States Courthouse in the City of New York, on the 1st day of June one thousand nine hundred and eighty-nine.

Present: HON. IRVING R. KAUFMAN,
HON. JON O. NEWMAN,
HON. ROGER J. MINER, *Circuit Judges.*

Docket No. 89-4030

INDEPENDENT INSURANCE AGENTS OF AMERICA, INC., *et al.*,
Petitioners,

-v-

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM,
Respondent.

[Filed June 1, 1989]

It is hereby ordered that the stay previously granted by this court shall continue pending disposition of the appeal.

ELAINE B. GOLDSMITH
Clerk

By: /s/ Arthur Heller
ARTHUR HELLER
Deputy Clerk

UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT

At a stated Term of the United States Court of Appeals for the Second Circuit, held at the United States Court-house in the City of New York, on the twenty eighth day of March one thousand nine hundred and eighty-nine.

Present: HON. WILFRED FEINBERG

HON. LAWRENCE W. PIERCE, Circuit Judges

HON. CONSTANCE BAKER MOTLEY, District Judge

Docket No. 89-4030

INDEPENDENT INSURANCE AGENTS OF AMERICA, INC., *et al.*,
Petitioners,

-v-

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM,
Respondent.

[Filed Mar. 28, 1989]

It is hereby ordered that the motion for a stay be and it hereby is GRANTED only until argument of the appeal.

The present scheduling order shall remain in effect.

ELAINE B. GOLDSMITH
Clerk

By: /s/ Edward J. Guardaro
EDWARD J. GUARDARO
Deputy Clerk

APPENDIX C

75 Fed. Res. Bull. 388 (1989)

FEDERAL RESERVE SYSTEM

Merchants National Corporation
Indianapolis, IndianaOrder Granting Relief From Commitments Regarding
Insurance Agency Activities of Subsidiary Banks

Merchants National Corporation, Indianapolis, Indiana ("Merchants"), a bank holding company within the meaning of the Bank Holding Company Act ("BHC Act" or "Act"), has applied under section 4(c)(8)(D) of the BHC Act (12 U.S.C. § 1843(c)(8)(D)) and section 225.25(b)(8)(iv) of the Board's Regulation Y (12 C.F.R. § 225.25(b)(8)(iv)) for approval for its wholly owned subsidiary, Anderson Banking Company, Anderson, Indiana ("Anderson Bank"), to resume the conduct of certain insurance agency activities authorized for state banks under Indiana law. Alternatively, Merchants seeks a Board determination that the nonbanking prohibitions of section 4 of the BHC Act do not apply to activities conducted directly by subsidiary banks of a bank holding company, thereby permitting Anderson Bank and another of Merchant's state bank subsidiaries, Mid State Bank of Hendricks County, Danville, Indiana ("Mid State Bank"), to resume insurance agency activities. In both cases the insurance agency activities would be conducted directly by the banks and not through subsidiaries of the banks.

I. Background

The record shows that Anderson Bank, prior to its acquisition by Merchants, engaged directly in insurance agency activities since the bank's incorporation in 1916

and that Mid State Bank acquired an insurance agency in 1985.¹ The banks are authorized to sell insurance directly pursuant to state law.²

On October 29, 1986, the Board approved applications by Merchants under section 3 of the BHC Act to acquire Anderson Bank and Mid State Bank. 72 Federal Reserve Bulletin 838 (1986). The applications had been protested by various insurance industry trade groups on the ground that, as subsidiaries of a bank holding company, the insurance agency activities then being conducted by the banks pursuant to Indiana law would be prohibited by section 4 of the BHC Act, as amended by Title VI of the Garn-St Germain Depository Institutions Act of 1982.³ As discussed below, the Garn-St Germain Act amended section 4(c)(8) of the BHC Act to provide that, with seven specific exceptions, insurance activities are not closely related to banking. This amendment removed the Board's discretion to authorize insurance activities as a permissible nonbanking activity for bank holding companies under the closely related to banking standard of section 4(c)(8) of the Act.

In response to the protests, Merchants committed that, unless it received Board approval in the meantime for the banks to retain their insurance activities, it would cause the banks to divest the insurance agency activities within two years and, in the interim, to refrain from the sale of insurance except for the renewal of existing poli-

¹ Prior to consummation of this proposal, Mid State Bank will transfer the insurance activities of the subsidiary to the bank itself, which will thereafter conduct the activities directly. Anderson Bank and Mid State Bank would act as agent for a full line of property and casualty coverage, but would not sell life insurance.

² Ind. Code § 28-1-11-2 provides that "any bank or trust company shall have power . . . to solicit and write insurance as agent or broker for any insurance company authorized to do business in this state, other than a life insurance company."

³ Pub. L. No. 97-320, codified at 12 U.S.C. § 1843(c)(8).

cies. Merchants subsequently sought relief from these commitments. On September 10, 1987, the Board granted the requested relief on the grounds that the insurance activities would be conducted directly by the banks and, thus, would not be prohibited by section 4 of the BHC Act or consequently the insurance provisions of the Garn-St Germain Act. 73 Federal Reserve Bulletin 876 (1987). The Board's Order noted that the relief did not violate the moratorium provisions of the Competitive Equality Banking Act of 1987 ("CEBA")⁴ because Merchants had acquired the banks involved before the moratorium. The Board also noted that the grant of relief would not increase the banks' insurance powers since the banks already had the powers by virtue of state law and those powers were not and never had been limited by the BHC Act.

Protestants sought review of the Board's decision in the United States Court of Appeals for the Second Circuit, which, on January 25, 1988, vacated the Board's Order.⁵ The court ruled that the Board's decision fell within the moratorium provisions of CEBA and, thus, that the Board should not have granted Merchants's request to conduct the insurance activities while the moratorium was effective. The court did not address the question of whether insurance activities conducted directly by the banks would be prohibited by the nonbanking provisions of section 4 of the BHC Act. The moratorium provisions have now expired, and Merchants has requested that the Board reissue the vacated Order.⁶

⁴ Pub. L. No. 100-86, 101 Stat. 552 (1987).

⁵ *Independent Insurance Agents of America, Inc. v. Board of Governors*, 838 F.2d 627 (2nd Cir. 1988).

⁶ By letter dated December 8, 1988, the Board granted a request by Merchants for an extension of time to divest the insurance agency activities of Anderson Bank and Mid State Bank until such time as the Board acts on the request of Merchants to reissue its earlier Order.

Notice of the application, affording interested persons an opportunity to submit comments on the proposal, was published (52 *Federal Register* 8966 (1987)). The time for filing comments has expired, and the Board has considered the application and all comments received, including those of various insurance trade associations ("protestants").⁷

Protestants contend that the banks do not qualify under any of the seven exemptions to the insurance provisions in the Garn-St Germain Act and that, therefore, they may not resume their insurance agency activities. With respect to Merchants's alternative argument, protestants contend that the terms and legislative history of the BHC Act and the Board's regulations indicate that the nonbanking and insurance provisions of section 4 of the BHC Act apply to all bank holding company activities, including activities conducted by a subsidiary bank of the holding company. In protestants' view, a bank holding company's activities, whether conducted directly by the holding company or by any of its subsidiaries, including subsidiary banks, are limited by the terms of section 4 of the Act to "banking" activities and activities permitted under the closely related to banking standard in section 4(c)(8) of the Act (or one of the other specific exemptions in the Act, none of which are relevant here). Protestants argue that because Anderson Bank's and Mid State Bank's insurance activities are not "banking" and do not qualify under any of the insurance ex-

⁷ The Board has received comments protesting the application and the request to reissue the earlier Order from the Independent Insurance Agents of America, Inc., Independent Insurance Agents of New York, Inc., National Association of Casualty and Surety Agents, National Association of Life Underwriters, National Association of Professional Insurance Agents, National Association of Surety Bond Producers, New York Association of Life Underwriters, and Professional Insurance Agents of New York, Inc.

emptions in section 4(c) (8), Merchants may not engage in the activities through the banks.⁸

After considering the comments of all interested parties and for the reasons set forth below, the Board has determined to grant Merchants's request for relief from its earlier commitments on the alternative grounds advanced by Merchants, thereby permitting Anderson Bank and Mid State Bank to resume the insurance agency activities they terminated when they were acquired by Merchants in 1986.

II. *Inapplicability of Exemption D of the Garn St-Germain Act*

Initially, the Board has determined that Anderson Bank and Mid State Bank do not qualify under section 4(c) (8) (D), the grandfather provision of the Garn-St Germain Act (hereinafter "exemption D"), to engage in insurance agency activities. Exemption D permits a bank holding company or any of its subsidiaries to engage in any insurance agency activity in which the bank holding company or subsidiary was engaged on May 1, 1982, sub-

⁸ Protestants also argue that Merchants should be bound by its earlier commitments to divest the banks' insurance activities because Merchants voluntarily offered the commitments with full knowledge of their limitations and that, in any event, the commitments preclude Merchants from arguing that the provisions of section 4 of the BHC Act do not apply to the direct activities of the banks.

In the Board's view, however, the commitments contemplated that Merchants could request Board relief from the commitments. While couched in terms of seeking Board approval on the Board's application Form Y-4, the commitments did not represent a concession by Merchants that section 4 applies to the direct activities of the banks. Rather, the commitments contemplated that the application would provide a forum for evaluating the issues and arguments raised by the proposal apart from Merchants' earlier application to acquire the banks. Accordingly, the Board does not consider that the commitments limit either the right of Merchants to request relief or the arguments Merchants may put forward in support of that relief.

ject to certain geographic and functional limitations. Exemption D, however, applies only to entities that were bank holding companies or subsidiaries of bank holding companies on May 1, 1982. The record shows that on May 1, 1982, Anderson Bank was not a subsidiary of a bank holding company and, therefore, does not qualify under Exemption D. Similarly, Mid State Bank does not qualify under Exemption D because it did not commence selling insurance until after the May 1, 1982, grandfather date.⁹

III. *Inapplicability of the Nonbanking Provisions of the BHC Act to the Direct Activities of Holding Company Banks*

Accordingly, the Board has considered Merchants's alternative ground for relief. On the basis of the record before it and the comments received, the Board has determined that the direct insurance activities of Anderson Bank and Mid State Bank are not limited by the nonbanking provisions of section 4 of the BHC Act or, consequently, the insurance provisions of the Garn-St Germain Act.¹⁰ In the Board's view, the nonbanking pro-

⁹ Mid State Bank appears to qualify for the exemption provided in section 4(c)(8)(C) of the BHC Act for insurance agency activities conducted in a town of less than 5,000 inhabitants. In this application, Merchants initially had proposed that Mid State Bank conduct the insurance agency activities through a wholly owned subsidiary under exemption C. Merchants, however, subsequently withdrew that request and amended the proposal to conduct the insurance activities directly by Mid State Bank on the basis discussed below that the nonbanking provisions of the BHC Act do not apply to the direct activities of holding company banks.

¹⁰ As noted, Title VI of the Garn-St Germain Act does not establish a prohibition on the conduct of insurance activities by bank holding companies separate from or in addition to the general nonbanking prohibitions of section 4 of the BHC Act. Rather, Title VI limits the Board's discretion to authorize bank holding companies to conduct these activities under the closely related to banking exception (in section 4(c)(8) of the Act) to the general nonbanking provisions of the Act (in section 4(a)). Thus, the provisions of the

visions of section 4 do not limit the *direct* activities of holding company banks, except where the record demonstrates the type of evasion described in the *Citicorp (South Dakota)* case,¹¹ a situation not present in the instant case.¹² The Board believes this view is consistent with the terms, purposes, and legislative history of the BHC Act and the Board's regulations, prior interpretations, and longstanding practice.

A. *Terms and Structure of the BHC Act*

Section 4 of the BHC Act contains two provisions that together limit the nonbanking activities and investments of bank holding companies. First, section 4 prohibits, with certain specific exceptions, a bank holding company from acquiring or retaining, directly or indirectly, voting shares of any company except a bank.¹³ The princi-

Garn-St Germain Act have no applicability to situations, such as this, where the nonbanking provisions of section 4 of the Act do not apply.

¹¹ 71 Federal Reserve Bulletin 789 (1985). In that case, the Board found, based on the structure of the South Dakota statute, the operating plans of Citicorp, and the fact that the bank would serve primarily as an insurance subsidiary of Citicorp and would conduct only insignificant banking activities, that the acquisition of the bank was primarily, if not solely, for the purpose of enabling Citicorp to engage through the bank in various insurance activities. The Board did not address the question raised in this case regarding whether the prohibitions of section 4 of the Act apply to the direct activities of holding company banks where no evidence of evasion is presented.

¹² In this case, the record does not show, nor is there any allegation, that the banks would be operated by Merchants predominantly as insurance agencies or that the acquisition of the banks is a device to enable the applicant to engage in insurance activities. Rather, the record shows that the insurance activities of the banks are incidental and small relative to their banking operations.

¹³ Section 4(a) of the Act provides:

Except as otherwise provided in this Act, no bank holding company shall

pal exception to this prohibition is for the shares of companies engaged in activities that the Board has determined are closely related to banking. By its terms, this restriction in section 4 does not apply to shares of a company that is itself a bank. Thus, a bank holding company that controls an institution that qualifies as a "bank" under the definition in the Act¹⁴ is not required, in order to acquire or retain the shares of the institution, to limit the institution's activities to those permitted under the closely related to banking standard of section 4 (or one of the other limited exceptions in the Act), except where the record demonstrates an evasion of the Act, such as presented in the *Citicorp (South Dakota)* case. It is only companies that do not qualify as "banks" under the Act that must limit their nonbanking activities to those permitted under the closely related to banking standard in section 4(c)(8) of the Act (or qualify under some other exception in section 4) in order to be acquired or retained directly or indirectly by a bank holding company.

In addition to the above limitation, section 4 of the Act provides that a bank holding company may not "engage in any activities other than . . . those of banking or of managing or controlling banks and other subsidiaries authorized under the Act or of furnishing services to or performing services for its subsidiaries" and activities the

(1) . . . acquire direct or indirect ownership or control of any voting shares of any company *which is not a bank*, or

(2) . . . retain direct or indirect ownership or control of any voting shares of any company *which is not a bank* or bank holding company or engage in any activities other than (A) those of banking or of managing or controlling banks and other subsidiaries authorized under this Act or of furnishing services to or performing services for its subsidiaries, and (B) those permitted under paragraph (8) of subsection (c) of this section [the closely related to banking exception] . . . (emphasis supplied) 12 U.S.C. § 1843(a).

¹⁴ 12 U.S.C. § 1841(c).

Board has determined to be closely related to banking. 12 U.S.C. § 1843(a)(2). Protestants contend that this provision applies not only to activities conducted directly by a bank holding company, but also to activities conducted indirectly through any subsidiary of the bank holding company, including a subsidiary bank. This interpretation, however, cannot be squared with the words or structure of the statute.

The language of the activities limitation in section 4(a)(2) forbids "bank holding companies"—not "banks"—from engaging in activities other than those specified in that provision. The BHC Act defines "bank holding company" to mean any company that has control over any bank,¹⁵ a definition that clearly refers only to the parent holding company itself, not to the system as a whole or to any "subsidiary," a term that is separately defined.¹⁶

The structure of the BHC Act indicates that this provision of section 4(a)(2) of the Act was intended to apply to the activities of bank holding companies themselves, many of which are operating companies engaged directly in nonbanking activities as well as in controlling banks and companies engaged in permissible nonbanking activities.¹⁷ This reading harmonizes the provisions of section 4 of the Act, with one provision limiting the types of companies the shares of which a bank holding company may acquire and retain (banks and other companies authorized under the Act), and the second limiting in a similar manner the activities in which the bank holding

¹⁵ 12 U.S.C. § 1841(a)(1).

¹⁶ 12 U.S.C. § 1841(d).

¹⁷ The portion of section 4 that authorizes a bank holding company to engage in "banking" is intended to provide for those few situations that existed in 1956 in which the bank holding company was itself a bank. See Heller, *Federal Bank Holding Company Law*, § 4.02(1).

company itself may engage to (1) banking, (2) managing and controlling banks and authorized nonbank companies, and (3) activities closely related to banking.

Furthermore, section 4(a) of the Act distinguishes between a bank holding company's acquiring and retaining "direct or indirect" ownership or control of any company that is not a bank, on the one hand, and the holding company's engaging in activities itself, on the other. The use of the words "direct or indirect" in the investment limitation of the Act makes clear that neither a bank holding company nor any of its subsidiaries may own or control a nonbank company (unless exempted). In the activities limitation of section 4(a)(2), however, Congress did not use the words "directly or indirectly" to modify the word "engage". This demonstrates, in the Board's view, Congress' intent to apply the activities limitation in section 4(a)(2) to the holding company only and not to its subsidiaries.¹⁸

The reading suggested by protestants would make superfluous the provision in section 4(a)(2) restricting the types of companies that may be controlled by bank holding companies to banks and authorized nonbanks. If a bank holding company is deemed to be engaged in each activity in which a company it controls is engaged, as protestants suggest, the other provision of section 4 prohibiting a bank holding company from controlling nonbank companies unless engaged in permissible activities

¹⁸ Protestants look to 12 U.S.C. § 1850, which establishes a competitor's standing to challenge adverse Board action regarding applications by bank holding companies to engage directly or indirectly in nonbanking activities, to demonstrate that the term "engage" in the BHC Act necessarily applies to the activities of a bank holding company and all its subsidiaries. In that section, however, the word "engage" is modified by the words "directly or indirectly." The activities limitation in section 4(a)(2), however, is not modified by the words "directly or indirectly."

would be unnecessary.¹⁹ Accordingly, the Board believes that the provision of section 4(a)(2) of the Act limiting the activities in which a bank holding company may "engage" applies only to the activities of the bank holding company itself, and that activities of subsidiaries of the bank holding company are regulated through provisions limiting the companies that a bank holding company may hold the shares of or control to banks and other companies engaged in activities permitted for bank holding companies under the Act.

Protestants point to the fact that a bank may be a "subsidiary" of a bank holding company under the Act's definition as evidence that the Act does not distinguish between banking and nonbanking subsidiaries.²⁰ That conclusion simply does not follow, however. The Act clearly distinguishes between banking and nonbanking subsidiaries in section 4(a) when it permits a bank holding company to control banks without any limitation on their activities, but provides that a bank holding company may control a "company which is not a bank" only if its activities are authorized under the closely related to banking or other nonbanking exceptions in the Act.²¹

¹⁹ Protestants suggest that Congress intentionally included a superfluous provision in order to establish a "catch-all" provision. The Board cannot accept this explanation, however, when the clear terms of the statute can be interpreted so as to give meaning to every word. See *Reiter v. Sonotone Corp.*, 442 U.S. 330, 339 (1979).

²⁰ 12 U.S.C. § 1841(d); also see 12 C.F.R. § 225.2(j).

²¹ With respect to the Board's definition of "subsidiary" in Regulation Y, the regulation makes clear that the definition does not apply where the context otherwise requires. 12 C.F.R. § 225.2.

Protestants also point to the fact that the insurance provisions in section 4(c)(8) begin by using the term "bank holding company" but then state in Exemption D that this limitation applies also to a bank holding company *and* its subsidiaries. On this basis, protestants argue, the reference in section 4(a)(2) to activities engaged in by a "bank holding company" must also refer to activi-

B. *Prior Board Interpretations*

Since enactment of the BHC Act, the Board has not read the nonbanking prohibitions of section 4 as applying to the direct activities of holding company banks. On the contrary, the Board's actions and regulations over the years have consistently interpreted section 4 as *not* applying to such bank activities.²² Protestants contend otherwise, pointing to section 225.21(a) of Regulation Y, which provides that "a bank holding company or a subsidiary may not engage in . . . any activity other than . . . an activity (permitted by section 4(c)(8))." The Board has never interpreted the provisions of Regulation Y relating to nonbanking activities as applicable to direct activities of banks, however.²³ For example, the Board

ties conducted by its subsidiaries, banking and nonbanking alike. As noted, however, section 4(c)(8) sets forth an exemption to the general prohibition found in section 4(a) against a bank holding company owning shares of a nonbank company. Because this general prohibition does not apply to shares of a bank, section 4(c)(8) must necessarily apply only to nonbank companies. Thus, in context and consistent with the prohibition in section 4, the reference in the insurance provisions to subsidiaries must mean subsidiaries to which the prohibition applies.

²² See, e.g., 12 C.F.R. § 225.118(c); *American Bancorp, Inc.*, 39 *Federal Register* 22,468 (June 24, 1974); *Piedmont Carolina Financial Services, Inc.*, 59 *Federal Reserve Bulletin* 766, 767-68 (1973); *Cameron Financial Corp. v. Board of Governors*, 497 F.2d 841, 845 (4th Cir. 1974); *Board of Governors v. Investment Company Institute*, 450 U.S. 46, 59 n.25 (1981); *Fed. Res. Reg. Serv.* 4-591 (Staff Op. January 12, 1982).

The Board notes that, contrary to protestants' implication, *Cameron* was not questioned by the Ninth Circuit ruling in *Patagonia Corp. v. Board of Governors*, 517 F.2d 803 (9th Cir. 1975), which distinguished *Cameron* and did not address the banking/nonbanking subsidiary issue. See 517 F.2d at 810-11 n.10.

²³ The original Regulation Y implementing the Act's provisions, adopted immediately after passage of the Act, contained no provision restricting the activities conducted directly by banks controlled by holding companies. 21 *Federal Register* 5686 (1956).

has never required bank holding companies that seek to acquire a bank to obtain prior approval under section 4(c)(8) for any nonbanking activities that might be engaged in directly by the bank, as would be required under protestants' construction of the statute. In addition, the section upon which protestants rely appears in a subpart of the Board's rules that pertains to the "*non-banking* acquisitions and activities of bank holding companies." Thus, in context and consistent with the terms of section 4(a) of the Act, the reference in section 225.21 (a) of Regulation Y to subsidiaries means subsidiaries other than banks.²⁴

²⁴ Protestants cite several isolated phrases from various regulations to argue that the Board has "repeatedly affirmed that bank holding companies and *all* of their subsidiaries are subject to section 4." None of the examples cited, however, are persuasive. First, the Board's requirement that courier services not be conducted through a servicing arm of the bank (12 C.F.R. § 225.129) was imposed to eliminate possible unfair competition and supports the view that the Board has no authority to authorize activities for banks under the BHC Act.

Second, the Board's now-repealed interpretive rule on insurance services (12 C.F.R. § 225.128) referred to bank subsidiaries of bank holding companies because bank holding companies were authorized to sell credit insurance in connection with loans made by both their bank and nonbank subsidiaries.

Third, soon after enactment of the Act, the Board issued an opinion making clear that the exemption provided by section 4(c)(6) of the Act (providing that the section 4(a) prohibitions shall not apply to the acquisition of less than five percent of the voting shares of a nonbanking company) applies to shares held by banking subsidiaries of a bank holding company as well as shares held directly by the bank holding company itself. 12 C.F.R. § 225.101. This position is consistent with section 4(a)'s prohibition against the direct and indirect ownership or control of shares of a nonbanking company. It says nothing about the application of the activities limitation of section 4(a)(2).

Finally, with respect to the Board's regulation relating to investment company advisory activities (12 C.F.R. § 225.125), the Board has made clear that while that regulation did define bank holding company to include both bank and nonbank subsidiaries,

C. *Legislative History and Purposes of the Statute*

The Board's reading of the scope of the section 4(a) prohibitions is fully consistent with the Act's legislative history. When the nonbanking prohibitions in section 4 were adopted in 1956 as part of the original Act, Congress gave no indication that the statute was meant to affect in any way the activities engaged in directly by holding company subsidiary banks, whose powers traditionally were determined by the authority that issued the bank's charter.²⁵

The 1970 amendment to section 4(c)(8) reinforced the view that section 4 does not reach the direct activities of banks controlled by holding companies. During proceedings on this amendment, Congress specifically considered and rejected a proposed amendment to section 4

"the restrictions contained in the interpretation on operations of banking subsidiaries were only intended to apply where the investment advisory function was being conducted by a nonbanking subsidiary of the bank holding company." Letter denying petition of Investment Company Institute, March 8, 1974.

²⁵ See S. Rep. No. 1095, Part 2, 84th Cong., 2d Sess. 5 (1956). The BHC Act does, however, provide the Board with certain supervisory authority over holding company banks. For example, the Board may examine any bank that is a subsidiary of a bank holding company (12 U.S.C. § 1844(c)) and is required to evaluate the management and financial condition of any bank that a bank holding company proposes to acquire (12 U.S.C. § 1842(c)).

Protestants argue that the Board's original *Merchants* decision is suspect because, according to protestants, the decision rested essentially on the premise that state banks are regulated exclusively by state law. Protestants have misread the Board's decision. As noted above, the Board recognizes that Congress intended for the OCC and the state banking authorities to remain as the *primary* (not exclusive) regulatory authorities responsible for their respective institutions. At the same time, the Board recognizes that the BHC Act provides the Board with certain supervisory authority over holding company banks. Second, the original decision, as well as the present one, rests on an interpretation of the explicit language of section 4 of the BHC Act.

that would have prohibited certain specified activities, including providing insurance, and that arguably applied to subsidiary banks as well as bank holding companies and their nonbank subsidiaries.²⁶

There is also no indication that when in 1982 Congress incorporated the general prohibition on approving insurance activities into section 4(c)(8), Congress meant to expand the general nonbanking prohibitions in section 4(a). The relevant history instead indicates that Congress intended to retain the existing regulatory framework contained in section 4. The Board has found no legislative history expressly stating that the Garn-St Germain Act was intended to limit the direct insurance activities of holding company banks.²⁷ To the contrary, the Board

²⁶ See 115 Cong. Rec. 33,133-34 (November 5, 1969); H.R. Rep. No. 387, 91st Cong., 1st Sess. 15 (1969); 115 Cong. Rec., E 9016-17 (daily ed. October 28, 1969) (statement of Rep. Brown); 115 Cong. Rec., H 10503 (daily ed. November 4, 1969) (statement of Rep. Stanton). *Bills to Amend the Bank Holding Company Act of 1956; Hearings on S. 1052, S. 1211, S. 1664, S. 3823, and H.R. 6778 Before the Senate Comm. on Banking and Currency, 91st Cong., 2nd Sess. 144, 157-158 (1970) (statement of Arthur Burns, Chairman of the Federal Reserve Board) (hereinafter cited as 1970 Senate hearings); 1970 Senate Hearings at 179-81 (Colloquy between Senator Packwood and Frank Wille, Chairman of the FDIC).*

²⁷ The Board has considered protestants' references to language from the Senate Conference Report on Title VI of the Garn-St Germain Act (S. Rep. No. 97-641, 97th Cong. 2d Sess. 91 (1982), which states that Title VI would prohibit "bank holding companies and their subsidiaries" from selling and underwriting insurance. In the Board's view, in the context of the terms of the Act, the purpose of the Garn-St Germain Act, and the longstanding practice of not applying the nonbanking provisions of the Act to the direct activities of holding company banks, the reference in the report to subsidiaries was meant to refer to nonbanking subsidiaries.

The Board notes that references in earlier reports on the Title VI legislation indicate that section 4 and thus the proposed legislation would apply to bank holding companies and their "nonbank subsidiaries." S. Rep. No. 96-923, 96th Cong., 2d Sess. 2 (1980); S. Rep. No. 97-536, 97th Cong., 2d Sess. 36, 38-40 (1982). See also,

explicitly advised Congress during Congressional hearings in 1980 that the draft legislation (containing substantially the same language as ultimately enacted) would not limit the insurance activities of subsidiary banks. In response to a question concerning whether "a bank owned by a bank holding company [would] be allowed to sell automobile casualty or collision insurance" under the proposed bill, the Board stated that the answer would depend on the state or federal chartering authority.²⁸ It is clear from the legislative reports that the Garn-St Germain Act was intended to address certain Board decisions under section 4(c)(8) that allowed bank holding companies to sell credit related property and casualty insurance.²⁹ These Board decisions clearly did not authorize any activities for the subsidiary banks of the companies involved.

The Board believes that reading the Garn-St Germain Act as inapplicable to the direct insurance activities of banks does not frustrate the basic remedial purposes of the Act, which were to address what Congress believed to be potential unfair competitive practices associated with provision of insurance by banking organizations. In this regard, the Board notes that prior to 1982 insurance

H.R. Rep. No. 96-845, 96th Cong., 2d Sess. 2-3 (1980) ("the BHC Act generally prohibits a bank holding company from owning the shares of any company that is not a bank.") There is no indication of any Congressional intent in the Title VI amendments to section 4(c)(8) of the Act to extend the coverage of the nonbanking prohibitions of section 4(a) of the Act to the direct activities of holding company banks.

²⁸ *Competition in Banking Act of 1980, Hearings Before the Senate Comm. on Banking, Housing and Urban Affairs, 96th Cong., 2d Sess. 22 (1980).*

²⁹ *See, e.g., S. Rep. No. 97-536, 97th Cong., 2d Sess. 36-37 (1982).* The Board, of course, has no authority to authorize state or national banks to conduct nonbanking activities. That authorization must come from the state banking authorities or the Comptroller of the Currency, respectively.

activities conducted directly by banks were not extensive, since banks were authorized to engage in these activities only in a few states and the acquisition of banks by out of state bank holding companies was not permitted. In contrast, under the Board's section 4(c)(8) decisions, on which Congress specifically focused in enacting the Garn-St Germain Act, insurance activities could be conducted by nonbank companies in a holding company system on a nationwide basis.³⁰

In any event, the Supreme Court has held that the purpose of legislation is determined in the first instance with reference to the plain language of the statute and that the broad purposes of legislation cannot be relied upon to overcome the terms of the statute itself.³¹ As

³⁰ After passage of the Garn-St Germain Act, in light of developments Congress could not necessarily have foreseen in 1982, the direct insurance activities of banks began to expand. The growth of interstate banking after the Supreme Court's decision in *North-east Bancorp, Inc. v. Board of Governors*, 472 U.S. 159 (1985), resulted in the establishment by bank holding companies of interstate networks of banks that could sell insurance. During this period there also was a general expansion in the powers of banks. Since 1982, Congress has repeatedly considered proposed legislation that would restrain the direct insurance functions of banks on a permanent basis, but no such legislation has been enacted.

³¹ *Board of Governors v. Dimension Financial Corporation*, 474 U.S. 361, 368, 373-374, (1986) ("If the statute is clear and unambiguous, 'that is the end of the matter, for the court, as well as the agency, must give effect to the unambiguously expressed intent of Congress.'" (citations omitted)). See also, *Independent Insurance Agents of America, Inc. v. Board of Governors*, 835 F.2d 1452, 1456-1457 (D.C. Cir. 1987). As the Supreme Court recognized, the process of legislative compromise may result in the adoption of express exceptions that run counter to the general remedial purpose of the legislation. 474 U.S. at 374. The legislative history of the Garn-St. Germain Act reveals some disagreement among members of Congress as to whether banking organizations should be prohibited completely from engaging in insurance activities. 128 Cong. Rec. S 12,220-24, 12,230 (1982).

noted, in this instance, the terms of the BHC Act are clear that the direct activities of holding company banks are not restricted by section 4 of the Act.

Protestants argue that failing to interpret section 4's activities limitation to apply to banking subsidiaries of a bank holding company will permit states to "nullify the effect" of the Act by permitting state banks to engage in nonbanking activities that are forbidden by section 4. In establishing the BHC Act framework, however, Congress was required to draw the line between banking and nonbanking activities in the Act in some manner. As the terms of the Act demonstrate, Congress rationally did so on the basis of whether the entity conducting the activity is a bank or a nonbank.³² Thus, where the company is chartered and operated as a bank under the definition in the BHC Act, it is outside the scope of the nonbanking provisions of the Act. But where the company is not a bank, it is, consistent with the line drawn by Congress in section 4, subject to the nonbanking provisions of the Act, and in order for these activities to be permissible, they must fit within one of the Act's authorizing provisions.

Protestants also rely on section 101(d) of CEBA, which amends section 3 of the BHC Act to permit qualified state-chartered savings banks to engage in any activity permitted by state law, but prohibits such savings banks from violating section 4(c)(8)'s insurance restrictions. 12 U.S.C. § 1842(f). Protestants assert that, if

³² Protestants point to several general references in the legislative history of the Act, as well as the 1966 and 1970 Amendments to the Act, to suggest that Congress intended to separate banking from nonbanking interests wherever the nonbanking interests were held, and that Congress intended for banks to divest themselves of their nonbanking interests. The Board agrees that one of the purposes of the BHC Act is to separate banking from commerce. As is evident in the terms and legislative history of the Act, Congress achieved this purpose by prohibiting banks from being affiliated within a bank holding company system with commercial companies.

section 4 did not restrict the nonbanking activities of banks, an exemption for savings bank would not have been necessary, nor would Congress have had any reason to apply the insurance restrictions uniquely to savings banks. Section 101(d), however, applies only to savings banks, which are not involved in this case, and does not extend the reach of section 4 of the BHC Act.

Moreover, it does not necessarily follow that this amendment to section 3 is an indication that Congress believed the restrictions in section 4 apply to all holding company banks. This amendment may have been intended merely to confirm, for this category of "banks," the Board's longstanding view that banks may engage in state-authorized activities in the face of contrary arguments advanced by insurance trade associations that the section 4 limitations apply to the direct activities of holding company banks. Congress' decision expressly to limit the insurance activities of these savings banks (in contrast to other types of holding company banks) is merely a part of a "special rule" adopted for those institutions under the BHC Act.³³ In fact, as noted, the 100th Congress actively considered (although it did not adopt) legislation expressly to extend these limitations to holding company banks—action that is inconsistent with protestants' interpretation of the Garn-St Germain Act.³⁴

For the foregoing reasons, the Board has determined that section 4 of the BHC Act does not limit the sale of insurance directly by Anderson Bank and Mid State Bank within the banks as proposed, and that the banks may,

³³ See H.R. Rep. No. 100-261, 100th Cong., 1st Sess. 130 (1987); S. Rep. No. 100-19, 100th Cong., 1st Sess. 33 (1987).

³⁴ Protestants' reliance on the nonbank bank provisions of CEBA also is misplaced. 12 U.S.C. § 1843(f). Such provisions were enacted in order to minimize the potential for unfair competition and adverse effects associated with the grandfather provisions applied to nonbank banks and their parent holding companies, not to expand the scope of the general prohibitions in section 4.

therefore, insofar as the BHC Act is concerned, resume within the banks the sale of insurance as permitted under Indiana law.³⁵

IV. *Operating Subsidiaries of State Banks*

The Board emphasizes that its views regarding the coverage of section 4 in this Order pertain only where the activities are conducted directly by banks. The Order does not address the situation where the insurance activities are conducted by nonbank companies controlled by holding company banks. Under the Act, shares of a company held by a holding company bank are deemed to be indirectly held by the parent holding company (12 U.S.C. § 1841(g)) and, therefore, under the terms of the Act, their ownership or control by a bank holding company must qualify under the closely related to banking exception or one of the other exceptions in section 4 of the Act.³⁶

³⁵ Protestants request that the Board take cognizance of the public interest questions involved in the issue of whether section 4 applies to activities conducted directly by state banks. The Board is required by section 4(c)(8), in determining whether a particular activity is closely related to banking, to consider whether its performance by a bank holding company affiliate can reasonably be expected to produce public benefits that outweigh possible adverse effects. Because the Board has determined that section 4's prohibitions do not apply to activities conducted by Merchants' state bank subsidiaries, the Board need not decide whether these activities are closely related to banking or that their performance meets the net public benefits test of section 4(c)(8). The Board notes, however, that the insurance activities of the banks will be subject to the anti-tying restrictions of the 1970 Amendments to the BHC Act, which unlike section 4(a) explicitly apply to "banks." 12 U.S.C. § 1972(1).

³⁶ Similarly, a bank holding company is deemed to control any company that is controlled by the holding company's subsidiaries. 12 U.S.C. § 1841(a)(2). Under section 4(a)(2) of the Act, in order for the holding company to maintain control of such a company, the company must be a "bank" or a company whose activities

In this regard, in 1971 the Board adopted section 225.22 (d) (2) of Regulation Y (formerly section 225.4(e)), which authorizes a state bank owned by a bank holding company to acquire and retain all (but not less than all) of the voting shares of a company, without Board approval under the Act, so long as the company engages solely in activities the parent bank may conduct directly and at locations at which the bank could conduct the activities. 12 C.F.R. § 225.22 (d) (2).³⁷ The Board adopted this regulation in order to permit holding company state banks to compete on equal footing with state banks that are not in a holding company system and in the absence of evidence that such acquisitions were resulting in evasions of the Act.³⁸ At that time, however, the Board stated that it would review the merits of the decision from time to time in light of its experience in administering the Act.³⁹

In December 1988, in light of a number of developments, the Board asked for comment on whether to rescind

qualify under one of the Act's nonbanking exceptions. 12 U.S.C. § 1843(a)(2).

³⁷ Section 225.22(d)(1) of Regulation Y authorizes a national bank to acquire and retain voting shares of a company in accordance with the rules of the Comptroller of the Currency. 12 C.F.R. § 225.22(d)(1).

³⁸ The regulation does not, as protestants assert, rest on the Board's "belief" that it has the authority to regulate the activities of subsidiary banks of bank holding companies.

³⁹ The Board stated:

The Board should not at this time apply the [nonbanking] restrictions [of the BHC Act] to subsidiaries of banks. This decision is believed warranted by considerations of equity between banks that are and are not members of bank holding companies and by the absence of evidence that acquisition by holding company banks are resulting in evasions of the purpose of the Act. The merits of this decision will be reviewed by the Board from time to time in light of its experience in administering the Act. (36 *Federal Register* 9292 (May 22, 1971)).

this regulation, thereby requiring bank holding companies to obtain approval under section 4(c)(8) of the BHC Act prior to establishing or acquiring, through their subsidiary state banks, shares of companies engaged in activities that the bank is permitted to conduct under state law, unless the transaction is otherwise authorized under the Act. 53 *Federal Register* 48,915 (1988). The comment period on the proposal ends April 28, 1989.⁴⁰

V. *Legislation Regarding Direct Activities of Holding Company Banks*

The Board notes that the 100th Congress had under active consideration legislation that would have applied the insurance prohibitions of the Garn-St Germain Act to the activities of holding company banks except where the bank was located in the same state as the bank holding company, the insurance activities were permissible under state law, and sales were limited to within the state. The insurance activities to be conducted by Merchants's subsidiary banks would not have been prohibited under these provisions. While this legislation was passed by the U.S. Senate and favorably reported by committees of the U.S. House of Representatives,⁴¹ no legislation was enacted into

⁴⁰ In December 1986, the Board asked for comment on whether to amend 12 C.F.R. § 225.22(d)(2) to prohibit bank holding companies from acquiring or retaining voting shares or control of companies engaged in real estate development activities or to limit such acquisitions to those situations that the Board proposed to permit for bank holding companies. 52 *Federal Register* 543, 551 (1987). The Board indicated that it would consider whether to apply the proposed restrictions to a wholly owned subsidiary of a holding company state bank. Contrary to protestants' implication, the proposed regulation would not bar state banks themselves that are owned by a holding company from engaging in state-authorized real estate activities within the bank.

⁴¹ S. 1886, Title VIII, § 802, 100th Cong., 2d Sess., 134 Cong. Rec. S3437 (daily ed. March 30, 1988); H.R. 5094, Title III, § 302, 100th Cong., 2d Sess., 134 Cong. Rec. H6453 (daily ed. August 4, 1988), 134 Cong. Rec. H8470 (Sept. 27, 1988). See also S. Rep. No.

law. The Board calls to Merchants's attention, however, that subsequent Congressional action may modify the Board's Order granting Merchants's request for relief without providing so-called grandfather rights to continue the insurance activities. The Board retains jurisdiction over the application to act to carry out the requirements of any legislation adopted by Congress that would affect the conduct of insurance activities by Merchants's subsidiary banks under the BHC Act.

VI. *Request for a Hearing*

Protestants have requested that the Board grant discovery rights and conduct a hearing under section 5(f) of the Act (12 U.S.C. § 1844(f)) on the application in order to determine whether Merchants is attempting to evade the BHC Act, as forbidden by the *Citicorp (South Dakota)* decision. However, section 5(f) does not itself require that a hearing be conducted in any case; this section merely sets forth the powers the Board may exercise in any hearing or other proceeding undertaken under another provision of the Act.

Section 4(c)(8) does provide that in approving activities under that provision the Board must provide notice and opportunity for hearing. However, because the Board has determined that section 4 does not apply to the direct activities of Merchants's subsidiary state banks, the Board by this Order is not approving an application under section 4(c)(8). Accordingly, protestants do not have the right to a hearing or discovery in this case, and the Board does not believe such a proceeding would be appropriate under the facts and circumstances of this case.⁴²

305, 100th Cong., 2d Sess., 108 (1988); H.R. Rep. No. 822 (Part 1), 100 Cong., 2d Sess., 166 (1988); H.R. Rep. No. 822 (Part 2), 100th Cong., 2d Sess., 80-81 (1988).

⁴² Even where the applicable provision requires an opportunity for a hearing, such as under section 4(c)(8), a protestant is not entitled to discovery and a hearing on every application, but only

By order of the Board of Governors,⁴³ effective March 3, 1989.

/s/ Jennifer J. Johnson
JENNIFER J. JOHNSON
Associate Secretary of
the Board

when there are material issues of fact in dispute. *Connecticut Bankers Assn. v. Board of Governors*, 627 F.2d 245 (D.C. Cir. 1980). In this case, there are no material issues of fact in dispute. Protestants present no specific allegations; rather, they assert that any evidence that might prove an evasive intent is in the hands of Merchants. Such a bare allegation is insufficient to show that material facts are in dispute. In any event, as noted above, the Board has determined that the factual basis for such evasion is not present in this case. Moreover, the Board retains supervisory authority to act under the BHC Act to prevent any evasion of the requirements of the Act or this order should that situation arise in the future.

⁴³ Voting for this action: Chairman Greenspan and Governors Johnson, Seger, Angell, Heller, Kelley, and LaWare.

APPENDIX D

UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT

At a stated term of the United States Court of Appeals for the Second Circuit, held at the United States Courthouse, in the City of New York, on the 18th day of January, one thousand nine hundred and Ninety.

Docket Number 89-4030

INDEPENDENT INSUR AGNTS

v.

Bd Govs FRS

[Filed Jan. 18, 1990]

A petition for rehearing containing a suggestion that the action be reheard in banc having been filed herein by counsel for the Petitioners, Independent Insurance Agents of America, Inc., Independent Insurance Agents of New York, Inc., New York State Assoc. of Life Underwriters and Professional Insurance Agents of New York, Inc.,

Upon consideration by the panel that heard the appeal, it is

Ordered that said petition for rehearing is DENIED.

It is further noted that the suggestion for rehearing in banc has been transmitted to the judges of the court in regular active service and to any other judge that heard the appeal and that no such judge has requested that a vote be taken thereon.

/s/ Elaine B. Goldsmith
ELAINE B. GOLDSMITH
Clerk

APPENDIX E

UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT

No. 559—August Term 1987

Argued: December 4, 1987 Decided: January 25, 1988

Docket No. 87-4118

INDEPENDENT INSURANCE AGENTS OF AMERICA, INC.,
—v.— *Petitioner,*

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM,
Respondent,

MERCHANTS NATIONAL CORPORATION, THE NATIONAL ASSOCIATION OF CASUALTY AND SURETY AGENTS, THE NATIONAL ASSOCIATION OF LIFE UNDERWRITERS, THE NATIONAL ASSOCIATION OF PROFESSIONAL INSURANCE AGENTS, and THE NATIONAL ASSOCIATION OF SURETY BOND PRODUCERS, *Intervenors.*

Before:

NEWMAN, CARDAMONE, and PIERCE,
Circuit Judges.

Petition for review of an order of the Board of Governors of the Federal Reserve System approving an application by a bank holding company to permit two of its bank subsidiaries to engage in insurance activities, notwithstanding the moratorium imposed by Title II of the Competitive Equality Banking Act of 1987.

Petition granted and order vacated.

JONATHAN B. SALLET, Wash., D.C. (Jamie S. Gorelick, Jay L. Alexander, Miller, Cassidy, Larroca & Lewin, Wash., D.C., on the brief), *for petitioner and insurance-agent intervenors.*

RICHARD M. ASHTON, Assoc. Gen. Counsel, Wash., D.C. (Richard K. Willard, Asst. Atty. Gen., U.S. Dept. of Justice, Wash., D.C.; Michael Bradfield, Gen. Counsel, Douglas B. Jordan, Bd. of Governors of Fed. Reserve System, Wash., D.C., on the brief), *for respondent.*

JAMES A. McDERMOTT, Indianapolis, Ind. (Stanley C. Fickle, Barnes & Thornburg, Indianapolis, Ind., on the brief) *for intervenor Merchants National Corporation.*

(Paul B. Galvania, Martin E. Lybecker, William L. Patton, Alan G. Priest, Mark P. Szpak, Ropes & Gray, Wash., D.C., filed a brief as amici curiae *for insurance company associations.*)

(John J. Gill, Gen. Counsel, Michael F. Crotty, Assoc. Gen. Counsel, American Bankers Assn., Wash., D.C., and Richard Whiting, Association of Bank Holding Companies, Wash., D.C., filed a brief as amici curiae *for American Bankers Association and Association of Bank Holding Companies.*)

(John L. Warden, H. Rodgin Cohen, Michael M. Wiseman, Laurretta E. Murdock, Charles S. Sullivan, Sullivan & Cromwell, New York, N.Y., filed a brief as amicus curiae *for New York Clearing House Association.*)

(Linley E. Pearson, Atty. Gen., J. Gordon Gibbs, Jr., Chief Counsel, Samuel L. Bolinger, Deputy Atty. Gen., Indianapolis, Ind., filed a brief as amicus curiae *for Indiana Dept. of Financial Institutions.*)

(James T. McIntyre, Jr., Leslie A. Dent, Hansell & Post, Wash., D.C., filed a brief as amicus curiae *for Insurance/Financial Affiliates of America, Inc.*)

(James F. Bell, Ernest Gellhorn, Carol R. Van Cleef, Imran M. Raschid, (Jones, Day, Reavis & Pogue, Wash., D.C., and Arthur E. Wilmarth, Jr., George Washington Univ. National Law Center, Wash., D.C., filed a brief as *amicus curiae for Conference of State Bank Supervisors.*)

JON O. NEWMAN, *Circuit Judge*:

The Independent Insurance Agents of America ("IIAA") petition for review of an order of the Board of Governors of the Federal Reserve System ("the Board" or "the Fed") permitting two Indiana state banks recently acquired by the Merchants National Corporation, a bank holding company, to resume specified insurance activities permitted under Indiana state law. The Board's approval rested upon a determination that the non-banking prohibitions of section 4 of the Bank Holding Company Act, as amended, 12 U.S.C. § 1843 (1982), do not apply to the insurance activities of the banking subsidiaries of bank holding companies. *Merchants National Corp.*, 73 Fed. Res. Bull. 876 (Sept. 10, 1987). For purposes of this appeal, the critical aspect of the Board's order is its conclusion that the order is not precluded by the moratorium Congress imposed upon federal banking agencies prohibiting for one year the approval of certain non-banking activities. The moratorium is contained in Title II of the Competitive Equality Banking Act of 1987 (CEBA), Pub. L. No. 100-86, §§ 201-205, 101 Stat. 552, 581-85 (1987) (to be codified at 12 U.S.C. § 1841 note). Section 201(b)(3) of the CEBA prohibits any federal banking agency from issuing, between March 6, 1987, and March 1, 1988, any rule, regulation, or order that would "have the effect of increasing the insurance powers" of any entity subject to the Bank Holding Company Act, and section 201(b)(4) specifically prohibits the Fed from approving the "acquisition" by a bank holding company of any entity, including a state-chartered bank, engaging in those insurance activities prohibited under sec-

tion 4 of the Bank Holding Company Act. We hold that the Board's *Merchants National* order is within the scope of the moratorium and therefore grant the petition for review and vacate the order.

The Statutory Framework

Before introducing the facts, it will be helpful to outline the pertinent statutory provisions of both the Bank Holding Company Act and the Competitive Equality Banking Act.

The Bank Holding Company Act of 1956. Though our disposition makes it unnecessary to rule on the Board's interpretation of section 4 of the Bank Holding Company Act, a brief mention of the Act's structure is appropriate as background. Briefly, the principal regulatory powers of the Fed under the Bank Holding Company Act are set forth in sections 3 and 4 of the Act. 12 U.S.C. §§ 1842, 1843. Section 3 requires Board approval of the acquisition of ownership or control of any bank by a bank holding company with narrow exceptions not here relevant.¹ Section 3 sets forth factors governing acquisition approval, focusing on the competitive effect of the proposed acquisition, the financial and managerial resources of both the holding company and the acquired bank, and the convenience and needs of the community served. 12 U.S.C. § 1842(c).

¹ Section 2 of the Act defines the term "bank holding company" in extensive detail, but for our purposes it may be understood simply as any company "which has control over any bank." 12 U.S.C. § 1841(a)(1). Until this year, a "bank" has been defined generally as any institution organized under state or federal law "which (1) accepts deposits that the depositor has a legal right to withdraw on demand, and (2) engages in the business of making commercial loans." 12 U.S.C. § 1241(c). Though not pertinent to the outcome of this appeal, it should be noted that this latter definition has been substantially amended by Title I of the Competitive Equality Banking Act of 1987, Pub. L. No. 100-86, § 101(a), 101 Stat. 552, 554.

Section 4 of the Act, the focal point of the Board's order in this case, regulates the non-banking activities of a bank holding company. Without intimating our views on the correctness of the Board's interpretation of the precise scope of section 4, it is sufficient to point out generally that section 4(a) prohibits a bank holding company from engaging in non-banking activities other than those permitted under section 4(c)(8) of the Act. Section 4(c)(8) sets forth the so-called "closely related to banking" exception to the non-banking provision. In relevant part, section 4(c)(8) states that the section 4(a) non-banking prohibitions shall not bar ownership by a bank holding company of:

shares of any company the activities of which the Board after due notice and opportunity for hearing has determined (by order or regulation) to be so closely related to banking or managing or controlling banks as to be a proper incident thereto, but for purposes of this subsection it is not closely related to banking or managing or controlling banks for a bank holding company to provide insurance as a principal, agent or broker . . .

12 U.S.C. § 1843(c)(8).

The Competitive Equality Banking Act of 1987. Title II of the CEBA² imposes a moratorium, effective between March 6, 1987, and March 1, 1988, on the exercise of federal banking agency authority relating to specified non-banking activities, including securities, real estate, and insurance activities of bank holding companies

² The other principal titles of the 1987 Act, among other things, amend the definition of the term "bank" as used in the Bank Holding Company Act (Title I), provide recapitalization for the Federal Savings and Loan Insurance Corporation (Title III), establish in the Federal Deposit Insurance Corporation emergency authority over failing banks (Title IV), clarify the role of the National Credit Union Administration (Title V), and set forth regulations relating to the practices of depository institutions delaying the availability of deposited funds (Title VI).

or their subsidiaries in order that Congress may have the opportunity to "conduct a comprehensive review of our banking and financial laws and to make decisions on the need for financial restructuring legislation in the light of today's changing financial environment . . . before the expiration of such moratorium." CEBA, § 203 (a).

That part of the moratorium statute relating to insurance activities of bank holding companies and their subsidiaries is divided into two primary substantive subsections. Section 201(b) (3) of Title II states:

A Federal banking agency may not issue any rule, regulation, or order that would have the effect of increasing the insurance powers of banks, bank holding companies, foreign banks or other companies subject to the Bank Holding Company Act of 1956 under section 8(a) of the International Banking Act of 1978, or banking or nonbanking subsidiaries thereof with respect to any activities in the United States, either with respect to specific banks or bank holding companies or subsidiaries thereof or generally beyond those expressly authorized for bank holding companies under subparagraphs (A) through (G) of section 4(c) (8) of the Bank Holding Company Act of 1956 (12 U.S.C. 1843(c) (8) (A) through (G)).

(Emphasis added).

Section 201(b) (4) contains the second moratorium provision relating to insurance, and specifically concerns the Fed. This provision states that during the moratorium period the Board

may not approve the acquisition by a bank holding company or by a foreign bank or other company subject to the Bank Holding Company Act of 1956 under section 8(a) of the International Banking Act of 1978, of any company, including a State-chartered

bank, unless the bank holding company, foreign bank, or other company has agreed to limit the insurance activities in the United States of the company to be acquired to those permissible under section 4(c)(8) of the Bank Holding Company Act of 1956.

(Emphasis added). Finally, section 202 of Title II states that nothing in the section 201 moratorium provisions is intended to prevent a regulated agency from issuing any rule, regulation, or order pursuant to preexisting legal authority "to expand the securities, insurance, or real estate powers of banks or bank holding companies . . . if the effective date of such rule, regulation, or order is delayed until the expiration" of the moratorium period, March 1, 1988.

The Facts

A number of states, including Indiana,³ historically have authorized state-chartered banks to provide insurance services to their customers. On July 1, 1986, Merchants National Corporation, a bank holding company within the meaning of the Bank Holding Company Act, 12 U.S.C. § 1841(a), sought permission from the Fed to acquire the stock of two banks chartered under the laws of the State of Indiana, the Anderson Banking Company ("Anderson Bank") and the Mid State Bank of Hendricks County ("Mid State Bank"). Both of these state banks had engaged in general insurance activities prior to the date of Merchants National's applications, Anderson Bank directly since its incorporation in 1916, and Mid State Bank since its purchase of an insurance agency in 1985.⁴

³ Ind. Code § 28-1-11-2 provides: "Any bank or trust company shall have power . . . to solicit and write insurance as agent or broker for any insurance company authorized to do business in this state, other than a life insurance company."

⁴ Merchants National subsequently made a commitment that Mid State Bank would transfer to itself all insurance activities from its insurance agency subsidiary and thereafter conduct all such activities directly in the bank.

The initial Merchants National applications were protested by various insurance industry trade groups, including the IIAA, on the ground that the provisions of section 4 of the Bank Holding Company Act apply to the insurance activities of state banks owned by bank holding companies and therefore that the acquisitions of Anderson Bank and Mid State Bank could not be approved without requiring termination of their insurance activities to the extent required under section 4. In response to the protests, Merchants National committed that it would cause the banks to divest their insurance agency activities within two years unless, within that time, it received Board approval for the banks to retain their insurance activities. Merchants National agreed that, prior to such approval, the banks would limit their insurance activities to the renewal of existing policies. In light of these commitments, the Board approved the applications on October 29, 1986. 72 Fed. Res. Bull. 838 (1986).

On February 5, 1987, Merchants National filed an application seeking Board approval for Anderson Bank and Mid State Bank to resume the insurance activities that had just been suspended pursuant to the acquisition commitments. Merchants National sought permission on two alternative grounds. First, it contended that Anderson Bank and Mid State Bank were exempt from the insurance provisions of section 4 of the Bank Holding Company Act pursuant to the "grandfather" provisions of section 4(c)(8)(D), as amended, under which a bank holding company or any of its subsidiaries is permitted to engage in insurance agency activity in which the holding company or the subsidiary was engaged on May 1, 1982, subject to certain geographical and functional limitations. Second, Merchants National sought more broadly a determination that the non-banking prohibitions of section 4 of the Act do not apply to activities conducted directly by banking subsidiaries of a bank holding company.

After giving interested parties an opportunity to comment, *see* 52 Fed. Reg. 8966, 8967 (March 20, 1987), the

Board on September 10, 1987, issued the order challenged on this appeal, permitting the two Indiana banks to resume their insurance activities. The Board ruled first that the grandfather provision in section 4(c)(8)(D) of the Bank Holding Company Act was inapplicable because that provision insulates only those entities that were bank holding companies or their subsidiaries as of May 1, 1982. Neither Anderson Bank nor Mid State Bank qualified under this provision. However, the Board agreed with Merchants' alternative contention that the section 4 prohibitions did not apply to the insurance activities of banking subsidiaries of bank holding companies.

• The Board made its September 10, 1987, order effective immediately. In doing so, the Board determined that the moratorium contained in the CEBA did not apply to its approval of Merchants National's application because the action neither "increas[ed] the insurance powers" of Merchants National or its banking subsidiaries in contravention of section 201(b)(3), nor "approve[d] the acquisition" of a bank in contravention of section 201(b)(4). On October 6, 1987, this Court entered a stay of the Board's order pending review.

Discussion

Our analysis begins and ends with consideration of the moratorium issue because we hold that the issuance of the Merchants National order violates the CEBA moratorium.

In construing the moratorium, we recognize the admonition of the Supreme Court that where a statute is "silent or ambiguous" with respect to a specific issue, a court should defer to the construction adopted by the agency administering the statute whenever the agency has adopted a "permissible construction of the statute." *Chevron U.S.A. Inc. v. Natural Resources Defense Council, Inc.*, 467 U.S. 837, 843 (1984) (footnote omitted). At the same time we also recognize that *Chevron* enjoins

courts to "give effect to the unambiguously expressed intent of Congress." *Id.* Though the classification of congressional intent as clear or ambiguous will sometimes be in the eye of the beholder, courts construing statutes enacted specifically to prohibit agency action ought to be especially careful not to allow dubious arguments advanced by the agency in behalf of its proffered construction to thwart congressional intent expressed with reasonable clarity, under the guise of deferring to agency expertise on matters of minimal ambiguity. See *Greater New York Hospital Ass'n v. Blum*, 634 F.2d 668, 673 (2d Cir. 1980) (agency view of statute more persuasive on issue that does not concern agency's jurisdiction). Congress enacted the CEBA moratorium to stop federal banking agencies from taking certain actions for a one-year interval so that Congress itself could have the opportunity to decide how to resolve certain controversies in the banking field. An enactment of that sort must not be given a crabbed interpretation that risks undermining its purpose.

Before examining in detail the two pertinent provisions of the moratorium, it is important to view them together in order to appreciate the evident purpose of Congress. Section 201(b)(4) prohibits the Board from approving a bank holding company's acquisition of a bank unless the acquired bank has agreed to limit its insurance activities to those permitted under section 4(c)(8) of the Bank Holding Company Act. Section 201(b)(3) prohibits any banking agency, including the Board, from issuing any order that has the effect of increasing the insurance powers of a bank holding company or its subsidiary banks. The combined effect of these two provisions is evident: no new insurance activities by bank holding companies or their bank subsidiaries during the moratorium by means of either acquisition of a bank already selling insurance or approval for a previously acquired bank to sell insurance. With this structure of the moratorium in mind, we turn to the Board's efforts to interpret each of

the moratorium provisions to permit the Merchants National order.

With respect to section 201(b)(4), the Board does not deny that this moratorium provision contemplates precisely the situation presented by the Merchants National application in all but one respect. Though section 201(b)(4) requires the Board to withhold approval of those activities specifically sought to be engaged in by the two bank subsidiaries of Merchants National, the Board points out that section 201(b)(4) applies only to Board approval of *acquisitions* of such banks so engaged. The Board's position is that because the state bank "acquisitions" were approved in 1986, before the beginning of the moratorium, approval of the subsequent application to resume suspended insurance activities is not subject to the terms of section 201(b)(4).

As applied to the circumstances of Merchants National's acquisitions of the Anderson and Mid State banks, we find the Board's reading of section 201(b)(4) untenable. The acquisitions, approved October 29, 1986, were conditioned upon a commitment by the holding company that the acquired state banks would cease their insurance activities within two years and severely curtail those activities in the interim. These commitments were understood to be necessary "in order to expedite Board approval for the acquisition of the banks," Brief of Respondent at 39. Though it is true that Merchants National's "acquisitions" were approved in a technical sense before the beginning of the moratorium, the reality is that the technique of granting acquisition approval subject to a commitment effectively split each acquisition into two parts, with the second aspect, the commitment, covering the rights to engage in insurance activities. This latter and, for present purposes, critical bundle of rights was not acquired until the commitment was lifted by the September 10, 1987, order under review, and that action was taken during the moratorium.

While we do not criticize the creative approach to expediting approval in this case, such creativity may not be used to thwart the congressional will by splitting an "acquisition" and thus evading the purpose of section 201(b)(4). It is particularly noteworthy that the commitments by Merchants National effectively to cease its acquired banks' insurance activities, which facilitated Board approval of the expedited acquisitions, are the very same conditions that section 201(b)(4) requires to make permissible an acquisition during the moratorium period that would otherwise be impermissible.⁵ The Board's present order completes the acquisitions by lifting conditions during a time when the moratorium requires those conditions to be imposed. We find the irony too much to bear and conclude that the Board's construction of the statutory language would permit an evasion of its purpose under the circumstances of this case.

Even were we to agree with the Board's reading of section 201(b)(4), we would in any event hold that its order is plainly covered by section 201(b)(3) of the moratorium. The Board contends that section 201(b)(3) does not apply because the order does not "increas[e] the insurance powers" of either Merchants National or the two Indiana subsidiary banks. The reason for this, argues the Board, is that the term "powers" is used in

⁵ Section 201(b)(4) states that the moratorium imposed by its terms shall not apply:

to the acquisition of a State-chartered bank by a bank holding company that on March 6, 1987, controlled one or more State-chartered banks that have engaged in insurance activities identical to those of the newly acquired institution so long as the bank holding company agrees that it will—

(A) within 2 years of the consummation of its acquisition of the State-chartered bank, divest or terminate that bank's impermissible insurance activities, and

(B) limit the bank's insurance activities during that 2 year period to the renewal of existing policies.

section 201(b)(3) in some technical or legal sense and that the ban on agency actions "increasing the insurance powers" of a regulated bank refers only to changes made in the bank's organic charter by the chartering authority. The Board supports this novel reading of the unmodified word "powers" by relying on its determination that under section 4 of the Bank Holding Company Act it has no authority to regulate the insurance activities of a state bank subsidiary, and concludes that its order is outside the scope of the "insurance powers" moratorium because Anderson Bank and Mid State Bank "already have these powers by virtue of state law and those powers are not and have never been limited by the [Bank Holding Company] Act." Order at 17, 73 Fed. Res. Bull. at 881.

This reading of the statute does not withstand scrutiny. To begin with, there is nothing in the statute to suggest that Congress intended only some technical meaning by its use of the word "powers." In fact, the phrase Congress used imposes a moratorium on agency action "that would have the *effect* of increasing the insurance powers," CEBA, § 201(b)(3) (emphasis added), suggesting a broad reading that gives the term "powers" a non-technical, functional meaning. Indeed, upon analysis the Board's reasoning is circular. The argument is that the moratorium applies only to insurance powers increased pursuant to the Board's legal authority, and because the Board believes it has no legal authority over state bank subsidiaries of bank holding companies under section 4 of the Bank Holding Company Act, the moratorium does not apply to its Merchants National order. The fault lies in the middle premise. Whatever the merits of the Board's view that section 4 excludes from the scope of its insurance prohibitions all bank subsidiaries of bank holding companies, the fact remains that the moratorium was enacted in part so that Congress could resolve precisely that issue. The insurance moratorium was imposed in

part due to disagreement over the nature and extent *under existing law* of those regulatory "powers" referred to by section 201(b)(3). Congress gave itself until March 1, 1988, to resolve this question free from agency action, and the Board may not ignore the congressional command on the ground that in its view the answer is clear. The scope of section 201(b)(3) must be left sufficiently capacious to include those agency actions bearing on matters withdrawn by Congress during the term of the moratorium.

The legislative history of the moratorium supports this understanding of those agency actions subject to its terms. One of the substantive issues Congress hoped to consider during the moratorium period is the so-called "South Dakota loophole."⁶ As the Senate Report explains:

Section 4(c)(8) [of the Bank Holding Company Act], as amended in 1982 by the Garn-St. Germain Act, limits the insurance activities of bank holding companies. The scope of those limitations is in dispute. All parties agree that the limitations apply to a bank holding company and its nonbank subsidiaries. Insurance industry groups contend that the limitations also apply to every bank controlled by a bank holding company, whereas bank holding companies contend that the limitations do not apply to banks. Pursuant to the latter argument, a major bank holding company sought to conduct insurance activities beyond those permissible under section 4(c)(8) through a State-chartered bank in South Dakota. Although that application [w]as denied, the

⁶ The phrase refers to a controversial South Dakota statute permitting a bank holding company to acquire a state bank for the purpose of engaging in insurance activities through the state bank. See *Citicorp/South Dakota*, 71 Fed. Res. Bull. 798 (1985).

so-called "South Dakota loophole" remains a source of controversy.

S. Rep. No. 19, 100th Cong., 1st Sess. 16, *reprinted in* 1987 U.S. Code Cong. & Admin. News 489, 506. *See also id.* at 44; H. Rep. No. 261, 100th Cong., 1st Sess. 148, *reprinted in* 1987 U.S. Code Cong. & Admin. News 588, 617. Though this discussion mentions the issue in the context of the acquisition provision of the moratorium, section 201(b)(4), rather than the increased powers provision, section 201(b)(3), it is clear from this legislative history that the Board's authority to regulate the insurance powers of state chartered banking subsidiaries of bank holding companies under current law was a matter of controversy in the first session of the 100th Congress, and this very controversy in part motivated passage of the moratorium. Whether Congress ultimately agrees or disagrees with the Board's interpretation of section 4 of the Bank Holding Company Act remains to be seen. But in light of the congressional intent to freeze agency action bearing on the contested issue until March 1, 1988, it would undermine the purpose of the moratorium to give it an artificially restricted interpretation, especially one that rests on a resolution of an issue that Congress has temporarily reserved for its own consideration.

Nor do we find persuasive the Board's reliance on section 201(d) and 201(e)(2) of the moratorium, which provide, respectively, that nothing in Title II shall "be construed to increase or reduce the insurance authority of bank holding companies or banking or nonbanking subsidiaries thereof or of national banks under current law" and that "neither the existence of the moratorium nor its expiration shall be construed to increase, decrease, or affect in any way the authority of State-chartered bank subsidiaries of bank holding companies with respect to insurance activities." These provisions

mean only that neither the fact of the moratorium's passage nor its terms should be understood to change existing laws as it relates to the "South Dakota loophole" debate.⁷ To rely on sections 201(d) and 201(e)(2) in interpreting the moratorium as if this debate never took place is to strip the moratorium's substantive provisions of all force, at least as they relate to state bank subsidiaries. In short, these provisions do not limit the scope of the moratorium itself.

There remains the question of relief. The Board, relying on section 202 of the CEBA, contends that even if the moratorium is applicable, "the order would not be invalid and the most IIAA would be entitled to is a stay of the order's effective date until the moratorium expires." Brief of Respondent at 47. We disagree. Section 202 permits an agency to issue rulings otherwise subject to the moratorium "if the effective date of such rule, regulation, or order is delayed until the expiration of such moratorium." The Board, however, did not delay the effective date of the Merchants National order, and we decline the invitation to amend the Board's order in order to preserve its validity. It should be unnecessary to remind the Board that the courts must not substitute their own judgment for that of the agency on matters of agency discretion. See *SEC v. Chenery Corp.*, 332 U.S. 194 (1947). We have no authority to predict that the Board, now advised that the moratorium applies to the approval of Merchants National's application, will choose to reissue its order with an effective date of March 1, 1988. The proper course is to vacate the order and permit the Board to proceed as it sees fit in a manner consistent with our decision and applicable law.

⁷ See 133 Cong. Rec. S3936 (daily ed. Mar. 26, 1987) (colloquy between Sen. Breaux and Sen. Proxmire); *id.* at S3939 (colloquy between Sen. Riegle and Sen. Proxmire); *id.* at S3957 (colloquy between Sen. Dodd and Sen. Proxmire).

In view of our disposition, it is both unnecessary and inappropriate for us to review that portion of the Board's order that concerns the scope of the non-banking prohibitions of section 4 of the Bank Holding Company Act.

The petition for review is granted, and the order of the Board is vacated.